

Before the  
Federal Communications Commission  
Washington, D.C. 20554

In the matter of	)	
	)	
Federal-State Joint Conference	)	WC Docket No. <u>02-269</u>
On Accounting Issues	)	
	)	
2000 Biennial Regulatory Review –	)	CC Docket No. 00-199
Comprehensive Review of the Accounting	)	
Requirements and ARMIS Reporting	)	
Requirements for Incumbent Local	)	
Exchange Carriers Phase II	)	
	)	
Jurisdictional Separations Reform and	)	CC Docket No. 80-286
Referral to the Federal-State Joint Board	)	
	)	
Local Competition and Broadband Reporting	)	CC Docket No. 99-301

### NOTICE OF PROPOSED RULEMAKING

**Adopted: December 17, 2003**

**Released: December 23, 2003**

**Comment Date: 30 days after Federal Register publication of this Notice**

**Reply Comment Date: 45 days after Federal Register publication of this Notice**

By the Commission

#### I. INTRODUCTION AND BACKGROUND

1. In this Notice of Proposed Rulemaking (Notice), we seek comment on the recommendations of the Federal-State Joint Conference on Accounting Issues (*Joint Conference*).<sup>1</sup> On October 9, 2003, the Joint Conference submitted the result of a year-long study of the Commission's accounting rules and on-going proceedings related to the Commission's accounting requirements. The Joint Conference Recommendation is attached to this Notice in its entirety.

2. On September 5, 2002, the Commission convened the Joint Conference "to provide a forum for an ongoing dialogue between the Commission and the states in order to ensure that regulatory accounting data and related information filed by carriers are adequate, truthful, and thorough."<sup>2</sup> The Commission found that the "Joint Conference will provide a focused means by which we and interested state commissions may conduct an open dialogue, collect and exchange information, and consider initiatives that will improve the collection of adequate, truthful, and thorough accounting data for regulatory purposes."<sup>3</sup> In charging the Joint Conference with the task of reexamining federal and state

<sup>1</sup> Letter from Federal-State Joint Conference on Accounting Issues to Marlene H. Dortch, Secretary, FCC (Oct. 9, 2003) (*Joint Conference Recommendation*) (submitting proposed recommendations to Commission's accounting rules). The *Joint Conference Recommendation* is contained in its entirety in Appendix A to this Notice.

<sup>2</sup> *Federal-State Joint Conference on Accounting Issues*, WC Docket No. 02-269, Order, 17 FCC Rcd 17025, 17025-27 paras. 1, 7 (2002) (*Convening Order*).

<sup>3</sup> *Convening Order*, 17 FCC Rcd at 17026 para. 4.

accounting and reporting requirements, the Commission noted that the Joint Conference has a broad mandate to perform its work, including the ability to recommend additions to, or eliminations of, accounting requirements.<sup>4</sup>

3. The Commission has considered modifications to its accounting rules on several occasions prior to establishing the Joint Conference and after the passage of the Telecommunications Act of 1996 (the 1996 Act). Most recently, in its Phase II proceeding, the Commission streamlined its Part 32 accounting requirements and Part 43 reporting requirements applicable to incumbent local exchange carriers (LECs).<sup>5</sup> As part of the 1998 biennial review, the Commission reduced certain accounting and reporting requirements.<sup>6</sup> Immediately after the 1996 Act, the Commission modified its existing accounting requirements to implement the statutory obligations of sections 260 and 271-276 of the Communications Act of 1934, as amended (the Act).<sup>7</sup> This Notice, however, represents the Commission's first opportunity to consider the recommendations of state commissions presented through the formal mechanism of the Joint Conference.

## II. DISCUSSION

4. The Joint Conference makes three categories of recommendations with respect to the Commission's accounting and reporting requirements.<sup>8</sup> First, the Joint Conference recommends maintaining or adding accounts and/or subaccounts to the Part 32 accounting requirements (and associated Part 43 ARMIS reporting requirements) that are used to monitor the finances of incumbent LECs. Second, the Joint Conference recommends certain modifications to the Commission's affiliate

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<sup>4</sup> *Id.* at 17027 para. 7. The Joint Conference sought comment on a range of accounting and reporting issues in a Public Notice. See Public Notice, *Federal-State Joint Conference on Accounting Issues Request for Comment*, WC Docket No. 02-269, 17 FCC Rcd 24902 (WCB 2002). In addition, the Joint Conference held a public hearing to gather information from a cross-section of telecommunications industry representatives. See Public Notice, *List of Panelists to Attend Public Hearing Held by the Federal-State Joint Conference on Accounting Issues*, 18 FCC Rcd 2532 (WCB 2003).

<sup>5</sup> 2000 Biennial Regulatory Review – Comprehensive Review of the Accounting Requirements and ARMIS Reporting Requirements for Incumbent Local Exchange Carriers. Phase II, Amendments to the Uniform System of Accounts for Interconnection, Jurisdictional Separations Reform and Referral to the Federal-State Joint Board, Local Competition and Broadband Reporting, Report and Order in CC Docket Nos. 00-199, 97-212, and 80-286; Further Notice of Proposed Rulemaking in CC Docket Nos. 00-199, 99-301, and 80-286, 16 FCC Rcd 19913 (2001) (*Phase II Order*).

<sup>6</sup> See 1998 Biennial Regulatory Review – Review of ARMIS Reporting Requirements, Report and Order, 14 FCC Rcd 11443 (1999) (*ARMIS Reductions Report and Order*), 1998 Biennial Regulatory Review – Review of Accounting and Cost Allocation Requirements, Report and Order, 14 FCC Rcd 11396 (1999) (*Accounting Reductions Order*).

<sup>7</sup> See *Accounting Safeguards Under the Telecommunications Act of 1996*, Report and Order, 11 FCC Rcd 17539 (1996) (*Accounting Safeguards Order*); *Accounting Safeguards Under the Telecommunications Act of 1996*, Second Order on Reconsideration, 15 FCC Rcd 1161 (2000).

<sup>8</sup> Under the Commission's Part 32 rules, incumbent LECs record their costs and revenues in the Uniform System of Accounts (USOA). 47 C.F.R. Part 32, see *Phase II Order*, 16 FCC Rcd at 19916-18 paras. 8-12 (describing Commission's accounting requirements). The Commission developed ARMIS, which stands for "Automated Reporting Management Information System," in 1987 to collect financial, operating, service quality, and network infrastructure information from certain incumbent LECs. See *Phase II Order*, 16 FCC Rcd at 19918-19 paras. 13-15; *Automated Reporting Requirements for Certain Class A and Tier 1 Telephone Companies (Parts 31, 43, 67, and 69 of the FCC's Rules)*, Order, 2 FCC Rcd 5770 (1987), modified on recon., Order on Reconsideration, 3 FCC Rcd 6375 (1988). In 1990, the Commission added reporting categories for service quality and infrastructure development. See *Policy and Rules Concerning Rates for Dominant Carriers*, Second Report and Order, 5 FCC Rcd 6786, 6827-30 (1990).

transactions rules.<sup>9</sup> Finally, the Joint Conference makes several recommendations on reporting certain operating data in ARMIS, and on clarifying which entities are subject to the Commission's accounting and reporting requirements

5 More specifically, the *Joint Conference Recommendation* makes the following proposals concerning the Commission's accounting and reporting requirements:<sup>10</sup>

(a) Modifying Part 32 Accounts

- The Commission should reinstate Account 5230, Directory Revenue,
- The Commission should maintain the disaggregation of Account 6621, Call Completion Services, Account 6622, Number Services, and Account 6623, Customer Services.
- The Commission should not implement the Phase II decision to consolidate the depreciation and amortization accounts, but rather maintain the disaggregation for Account 6561, Depreciation Expense – Telecommunications Plant in Service, Account 6562, Depreciation Expense – Property Held for Future Telecommunications, Account 6563, Amortization Expense – Tangible, Account 6564, Amortization Expense – Intangible, and Account 6565, Amortization Expense – Other.
- The Commission should add accounts to its Part 32 Uniform System of Accounts to obtain information on the following subjects: (i) optical switching; (ii) switching software; (iii) loop and interoffice transport; (iv) interconnection revenue (with subaccounts for unbundled network elements, resale, reciprocal compensation, and interconnection arrangements), (v) universal service support revenue; and (vi) universal service support expense

(b) Affiliate Transactions

- The Commission should maintain the requirement for a comparison between net book cost and fair market value for the first \$500,000 of asset transfers
- The Commission should modify its rules to prevent incumbent LECs from valuing the cost of certain affiliate transactions, in accordance with the floor/ceiling approach adopted in the *Phase II Order*.

<sup>9</sup> See 47 C.F.R. § 32.27, see *Phase II Order*, 16 FCC Rcd at 19946-52 paras. 85-100; *Accounting Safeguards Order*, 11 FCC Rcd at 17582-17619 paras. 101-170. The Joint Conference also recommends that the Commission adopt, under our general authority, separate affiliate, accounting and auditing requirements focused on the in-region interLATA telecommunications service operations of the Bell Operating Companies (BOCs). *Joint Conference Recommendation* at 27-31. In May 2002, the Commission sought comment on a similar proposal in a proceeding devoted to considering the implications of the sunset of section 272 requirements. *Section 272(f)(1) Sunset of the BOC Separate Affiliate and Related Requirements*, WC Docket No. 02-112, Further Notice of Proposed Rulemaking, 18 FCC Rcd 10914, 10936-37 para. 46 (2003) (asking whether separate affiliate requirements are appropriate to apply to BOCs after sunset of section 272). The Joint Conference Recommendation has been entered into WC Docket No. 02-112 as an *ex parte* filing for consideration by the participants in that proceeding. Accordingly, the Joint Conference Recommendation on this subject will be resolved in WC Docket No. 02-112, and we do not seek comment on this aspect of the Joint Conference's recommendation in the instant Notice.

<sup>10</sup> See *infra* App. A

- The Commission should raise the qualification threshold for using the method of prevailing price valuation of affiliate transactions, from 25 percent to 50 percent
- The Commission should eliminate the exemption for central services organizations
- The Commission should maintain the existing reporting requirements for nonregulated-to-nonregulated affiliate transactions
- The Commission should apply the affiliate transactions rules to transactions between incumbent LECs within the same holding company.

(c) Reporting Requirements and Other Issues

- If the Commission chooses to collect local loop facility information as "Loop Sheath Kilometers" in the ARMIS 43-07 Infrastructure Report, the Commission should also reinstate the reporting of sheath kilometers.
- The Commission should require incumbent LECs to report data about their deployment of hybrid fiber/copper local loops in the ARMIS 43-07 Infrastructure Report
- The Commission should apply its accounting and reporting requirements to all incumbent LECs, as that term is defined in section 251(h) of the Act.

6. We seek comment on the proposals of the Joint Conference. We note that the Joint Conference prepared its recommendation based on an understanding that the Commission has authority to adopt accounting and reporting requirements in the absence of a federal need. In other words, the Joint Conference asserts that the Commission has the authority to adopt accounting and reporting requirements to meet the needs of state regulatory commissions and other stakeholders. We seek comment on this aspect of the *Joint Conference Recommendation*.

7. We also invite parties to comment on the Commission's accounting and reporting requirements in general. To the extent that parties propose to modify, add or eliminate any accounting or reporting requirements, they should describe their proposals with specificity (including the benefits), explain the grounds for making any such changes, and estimate the burden on carriers and other industry stakeholders (e.g., state commissions). We also invite parties to recommend specific areas of investigation or study by the Joint Conference as it continues to perform its duties.

8. The Commission previously has delayed implementation of certain modifications adopted in the Phase II proceeding in order to afford the Joint Conference time to consider them.<sup>11</sup> The rules were scheduled to go into effect on January 1, 2004, well before the Commission meaningfully can consider the comments filed pursuant to this Notice. We therefore seek comment on further delaying

<sup>11</sup> *Federal-State Joint Conference on Accounting Issues*, Order, 17 FCC Rcd 23243 (2002) (suspending implementation until July 1, 2003) (*First Suspension Order*), *Federal-State Joint Conference on Accounting Issues*, Order, 18 FCC Rcd 12636 (2003) (further suspending implementation until January 1, 2004) (*Second Suspension Order*). The following rule changes were suspended by these two orders: (1) consolidation of Accounts 6621 through 6623 into Account 6620, with sub-accounts for wholesale and retail, (2) consolidation of Account 5230, Directory Revenue, into Account 5200, Miscellaneous Revenue, (3) consolidation of the depreciation and amortization expense accounts (Accounts 6561 through 6565) into Account 6562, Depreciation and Amortization Expenses, and (4) revised "Loop Sheath Kilometers" data collection in Table II of ARMIS Report 43-07.

implementation until January 1, 2005, which is the next date to coincide with the start of a fiscal year after the former January 1, 2004 effective date. In a separate Order, we are extending the current suspension through June 30, 2004 to allow time for receipt and consideration of comments on this matter.<sup>12</sup>

### III. PROCEDURAL MATTERS

#### A. Regulatory Flexibility Act

9 As required by the Regulatory Flexibility Act of 1980, as amended (RFA),<sup>13</sup> the Commission has prepared this Initial Regulatory Flexibility Analysis (IRFA) of the possible significant economic impact on a substantial number of small entities by the policies and rules proposed in this Notice. Written public comments are requested on this IRFA. Comments must be identified as responses to the IRFA and must be filed by the deadlines for comments on the Notice provided below in Section C. The Commission will send a copy of the Notice, including this IRFA, to the Chief Counsel for Advocacy of the Small Business Administration (SBA).<sup>14</sup> In addition, the Notice and IRFA (or summaries thereof) will be published in the Federal Register.<sup>15</sup>

##### 1. Need for, and Objectives of, the Proposed Rules

10 The Commission has initiated this Notice to seek comment on the recommendations of the Federal-State Joint Conference on Accounting Issues (Joint Conference). The Commission created the Joint Conference so that the Commission and the states cooperatively may review regulatory accounting, and related reporting requirements, for adequacy and effectiveness. On October 9, 2003, the Joint Conference made several recommendations related to the Part 32 Accounts, the affiliate transactions rules, reporting requirements, and clarification on which entities are subject to the Commission's accounting and reporting requirements. More specifically, the Joint Conference recommends that the Commission modify its Part 32 rules by reinstating Account 5230 and maintaining the disaggregation of Accounts 6621, 6622 and 6623, and of accounts 6561, 6562, 6563, 6564 and 6565. The Joint Conference also recommends that the Commission add several new accounts to the Part 32 rules.

11 Under the Commission's rules, there are two classes of incumbent LECs for accounting purposes: Class A and Class B. Carriers with annual revenues from regulated telecommunications operations that are equal to or above the indexed revenue threshold, currently \$121 million, are classified as Class A, those falling below that threshold are considered Class B. Class A carriers are required to maintain 164 Class A accounts while Class B carriers are required to maintain only 89 accounts. Moreover, Class A carriers with annual revenues in excess of \$121 million but less than \$7.083 billion are classified as mid-sized carriers and are permitted to maintain accounts at the Class B level. The new accounts proposed by the Joint Conference for Part 32, and those proposed for reinstatement in Part 32, would apply only to Class A accounts.

12. The Joint Conference recommends changes to regulatory and reporting requirements for affiliate transactions. It also makes recommendations concerning the applicability of these requirements.

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<sup>12</sup> *Federal-State Joint Conference on Accounting Issues*, Order, FCC 03-325 (rel. Dec. 23, 2003) (further suspending implementation through June 30, 2004) (*Third Suspension Order*).

<sup>13</sup> See 5 U.S.C. § 603. The RFA, see 5 U.S.C. § 601 *et seq.*, has been amended by the Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA), Pub. L. No. 104-121, Title II, 110 Stat. 857 (1996).

<sup>14</sup> See 5 U.S.C. § 603(a).

<sup>15</sup> *Id.*

to certain types of affiliate transactions. These recommendations on affiliate transactions apply to both Class A and Class B carriers

13. Finally, the Joint Conference recommends changes to the Commission's ARMIS reporting requirements, including their applicability to certain types of carriers. The Joint Conference also recommends that all ILECs, not just dominant ILECs, be subject to the Commission's reporting classification in section 32.11 of its rules, 47 C.F.R. § 32.11

## **2. Legal Basis**

14. This Notice is supported by sections 1, 4(i), (4j), 201-205, 219, 220, 251, 252 and 303 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 154(i), (j), 201-205, 251, 252 and 303.

## **3. Description and Estimate of the Number of Small Entities to which the Proposed Rules Will Apply**

15. The RFA directs agencies to provide a description of and, where feasible, an estimate of the number of small entities that will be affected by the proposed rules.<sup>16</sup> The RFA generally defines the term "small entity" as having the same meaning as the terms "small business," "small organization," and "small governmental jurisdiction."<sup>17</sup> In addition, the term "small business" has the same meaning as the term "small business concern" under the Small Business Act.<sup>18</sup> A small business concern is one which (1) is independently owned and operated; (2) is not dominant in its field of operation; and (3) satisfies any additional criteria established by the Small Business Administration (SBA).<sup>19</sup> The term "small governmental jurisdiction" is defined as "governments of cities, towns, townships, villages, school districts, or special districts, with a population of less than fifty thousand."<sup>20</sup> As of 1997, there were about 87,453 governmental jurisdictions in the United States.<sup>21</sup> This number includes 39,044 county governments, municipalities, and townships, of which 37,546 (approximately 96.2%) have populations of fewer than 50,000, and of which 1,498 have populations of 50,000 or more. Thus, we estimate the number of small governmental jurisdictions overall to be 84,098 or fewer. We also note that the term "small governmental jurisdiction" includes state regulatory bodies commonly known as state public utilities commissions or public service commissions, which may be directly affected by this NPRM.

16. In this section, we further describe and estimate the number of small entity licensees and regulatees that may also be directly affected by rules adopted pursuant to this NPRM. The most reliable source of information regarding the total numbers of certain common carrier and related providers nationwide, as well as the number of commercial wireless entities, appears to be the data that the

<sup>16</sup> 5 U.S.C. §§ 603(b)(3), 604(a)(3).

<sup>17</sup> *Id.* § 601(6)

<sup>18</sup> *Id.* § 601(3) (incorporating by reference the definition of "small business concern" in the Small Business Act, 15 U.S.C. § 632). Pursuant to 5 U.S.C. § 601(3), the statutory definition of a small business applies "unless an agency, after consultation with the Office of Advocacy of the Small Business Administration and after opportunity for public comment, establishes one or more definitions of such terms which are appropriate to the activities of the agency and publishes such definitions(s) in the Federal Register."

<sup>19</sup> 15 U.S.C. § 632

<sup>20</sup> 5 U.S.C. § 601(5)

<sup>21</sup> U.S. Census Bureau, *Statistical Abstract of the United States 2000*, Section 9, pages 299-300, Tables 490 and 492

Commission publishes in its *Trends in Telephone Service* report<sup>22</sup> The SBA has developed small business size standards for wireline and wireless small businesses within the three commercial census categories of Wired Telecommunications Carriers,<sup>23</sup> Paging,<sup>24</sup> and Cellular and Other Wireless Telecommunications.<sup>25</sup> Under these categories, a business is small if it has 1,500 or fewer employees. Below, using the above size standards and others, we discuss the total estimated numbers of small businesses that might be affected by our actions.

17 We have included small incumbent LECs in this present RFA analysis. As noted above, a "small business" under the RFA is one that, *inter alia*, meets the pertinent small business size standard (e.g., a wired telecommunications carrier having 1,500 or fewer employees), and "is not dominant in its field of operation."<sup>26</sup> The SBA's Office of Advocacy contends that, for RFA purposes, small incumbent LECs are not dominant in their field of operation because any such dominance is not "national" in scope.<sup>27</sup> We have therefore included small incumbent LECs in this RFA analysis, although we emphasize that this RFA action has no effect on Commission analyses and determinations in other, non-RFA contexts.

18 *Wired Telecommunications Carriers* The SBA has developed a small business size standard for Wired Telecommunications Carriers, which consists of all such companies having 1,500 or fewer employees.<sup>28</sup> According to Census Bureau data for 1997, there were 2,225 firms in this category, total, that operated for the entire year.<sup>29</sup> Of this total, 2,201 firms had employment of 999 or fewer employees, and an additional 24 firms had employment of 1,000 employees or more.<sup>30</sup> Thus, under this size standard, the majority of firms can be considered small.

19 *Incumbent Local Exchange Carriers (LECs)*. Neither the Commission nor the SBA has developed a size standard for small businesses specifically applicable to incumbent local exchange services. The closest applicable size standard under SBA rules is for Wired Telecommunications Carriers. Under that size standard, such a business is small if it has 1,500 or fewer employees.<sup>31</sup> According to Commission data,<sup>32</sup> 1,337 carriers reported that they were engaged in the provision of local

<sup>22</sup> FCC, Wireline Competition Bureau, Industry Analysis and Technology Division, *Trends in Telephone Service*, Table 5.3 (August 2003) (*Trends in Telephone Service*).

<sup>23</sup> 13 C.F.R. § 121.201, North American Industry Classification System (NAICS) code 513310 (changed to 517110 in October 2002).

<sup>24</sup> *Id.* § 121.201, NAICS code 513321 (changed to 517211 in October 2002).

<sup>25</sup> *Id.* § 121.201, NAICS code 513322 (changed to 517212 in October 2002).

<sup>26</sup> 5 U.S.C. § 601(3).

<sup>27</sup> Letter from Jere W. Glover, Chief Counsel for Advocacy, SBA, to William E. Kennard, Chairman, FCC (May 27, 1999). The Small Business Act contains a definition of "small business concern," which the RFA incorporates into its own definition of "small business." See 15 U.S.C. § 632(a), 5 U.S.C. § 601(3). SBA regulations interpret "small business concern" to include the concept of dominance on a national basis. 13 C.F.R. § 121.102(b).

<sup>28</sup> 13 C.F.R. § 121.201, NAICS code 513310 (changed to 517110 in October 2002).

<sup>29</sup> U.S. Census Bureau, 1997 Economic Census, Subject Series: Information, "Establishment and Firm Size (Including Legal Form of Organization)," Table 5, NAICS code 513310 (issued October 2000).

<sup>30</sup> *Id.* The census data do not provide a more precise estimate of the number of firms that have employment of 1,500 or fewer employees; the largest category provided is "Firms with 1,000 employees or more."

<sup>31</sup> 13 C.F.R. § 121.201, NAICS code 513310 (changed to 517110 in October 2002).

<sup>32</sup> *Trends in Telephone Service* at Table 5.3.

exchange services. Of these 1,337 carriers, an estimated 1,032 have 1,500 or fewer employees and 305 have more than 1,500 employees. Consequently, the Commission estimates that most providers of incumbent local exchange service are small businesses that may be affected by the rules and policies adopted herein.

20 *Competitive Local Exchange Carriers (CLECs).* Neither the Commission nor the SBA has developed a size standard for small businesses specifically applicable to providers of competitive exchange services or to competitive access providers or to "Other Local Exchange Carriers," all of which are discrete categories under which TRS data are collected. The closest applicable size standard under SBA rules is for Wired Telecommunications Carriers. Under that size standard, such a business is small if it has 1,500 or fewer employees.<sup>33</sup> According to Commission data,<sup>34</sup> 609 companies reported that they were engaged in the provision of either competitive access provider services or competitive local exchange carrier services. Of these 609 companies, an estimated 458 have 1,500 or fewer employees and 151 have more than 1,500 employees.<sup>35</sup> In addition, 35 carriers reported that they were "Other Local Service Providers." Of the 35 "Other Local Service Providers," an estimated 34 have 1,500 or fewer employees and one has more than 1,500 employees.<sup>36</sup> Consequently, the Commission estimates that most providers of competitive local exchange service, competitive access providers, and "Other Local Exchange Carriers" are small entities that may be affected by the rules and policies adopted herein.

21 *Interexchange Carriers (IXCs).* Neither the Commission nor the SBA has developed a size standard for small businesses specifically applicable to interexchange services. The closest applicable size standard under SBA rules is for Wired Telecommunications Carriers. Under that size standard, such a business is small if it has 1,500 or fewer employees.<sup>37</sup> According to Commission data,<sup>38</sup> 261 companies reported that their primary telecommunications service activity was the provision of interexchange services. Of these 261 companies, an estimated 223 have 1,500 or fewer employees and 38 have more than 1,500 employees.<sup>39</sup> Consequently, the Commission estimates that the majority of interexchange service providers are small entities that may be affected by the rules and policies adopted herein.

22 *Operator Service Providers (OSPs).* Neither the Commission nor the SBA has developed a size standard for small businesses specifically applicable to operator service providers. The closest applicable size standard under SBA rules is for Wired Telecommunications Carriers. Under that size standard, such a business is small if it has 1,500 or fewer employees.<sup>40</sup> According to Commission data,<sup>41</sup> 23 companies reported that they were engaged in the provision of operator services. Of these 23 companies, an estimated 22 have 1,500 or fewer employees and one has more than 1,500 employees.<sup>42</sup> Consequently, the Commission estimates that the majority of operator service providers are small entities that may be affected by the rules and policies adopted herein.

<sup>33</sup> 13 C.F.R. § 121.201, NAICS code 513310 (changed to 517110 in October 2002).

<sup>34</sup> *Trends in Telephone Service* at Table 5.3.

<sup>35</sup> *Id.*

<sup>36</sup> *Id.*

<sup>37</sup> 13 C.F.R. § 121.201, NAICS code 513310 (changed to 517110 in October 2002).

<sup>38</sup> *Trends in Telephone Service* at Table 5.3.

<sup>39</sup> *Id.*

<sup>40</sup> 13 C.F.R. § 121.201, NAICS code 513310 (changed to 517110 in October 2002).

<sup>41</sup> *Trends in Telephone Service* at Table 5.3.

<sup>42</sup> *Id.*



23 *Payphone Service Providers (PSPs)* Neither the Commission nor the SBA has developed a size standard for small businesses specifically applicable to payphone services providers. The closest applicable size standard under SBA rules is for Wired Telecommunications Carriers. Under that size standard, such a business is small if it has 1,500 or fewer employees.<sup>43</sup> According to Commission data,<sup>44</sup> 761 companies reported that they were engaged in the provision of payphone services. Of these 761 companies, an estimated 757 have 1,500 or fewer employees and four have more than 1,500 employees.<sup>45</sup> Consequently, the Commission estimates that the majority of payphone service providers are small entities that may be affected by the rules and policies adopted herein.

24 *Prepaid Calling Card Providers* The SBA has developed a size standard for a small business within the category of Telecommunications Resellers. Under that SBA size standard, such a business is small if it has 1,500 or fewer employees.<sup>46</sup> According to Commission data,<sup>47</sup> 37 companies reported that they were engaged in the provision of prepaid calling cards. Of these 37 companies, an estimated 36 have 1,500 or fewer employees and one has more than 1,500 employees.<sup>48</sup> Consequently, the Commission estimates that the majority of prepaid calling card providers are small entities that may be affected by the rules and policies adopted herein.

25 *Other Toll Carriers*. Neither the Commission nor the SBA has developed a size standard for small businesses specifically applicable to "Other Toll Carriers." This category includes toll carriers that do not fall within the categories of interexchange carriers, operator service providers, prepaid calling card providers, satellite service carriers, or toll resellers. The closest applicable size standard under SBA rules is for Wired Telecommunications Carriers. Under that size standard, such a business is small if it has 1,500 or fewer employees.<sup>49</sup> According to Commission's data,<sup>50</sup> 92 companies reported that their primary telecommunications service activity was the provision of other toll carriage. Of these 92 companies, an estimated 82 have 1,500 or fewer employees and ten have more than 1,500 employees.<sup>51</sup> Consequently, the Commission estimates that most "Other Toll Carriers" are small entities that may be affected by the rules and policies adopted herein.

26 *Wireless Service Providers* The SBA has developed a small business size standard for wireless firms within the two broad economic census categories of Paging<sup>52</sup> and Cellular and Other Wireless Telecommunications.<sup>53</sup> Under both SBA categories, a wireless business is small if it has 1,500 or fewer employees. For the census category of Paging, Census Bureau data for 1997 show that there were 1320 firms in this category, total, that operated for the entire year.<sup>54</sup> Of this total, 1303 firms had

<sup>43</sup> 13 C.F.R. § 121.201, NAICS code 513310 (changed to 517110 in October 2002).

<sup>44</sup> *Trends in Telephone Service* at Table 5.3.

<sup>45</sup> *Id.*

<sup>46</sup> 13 C.F.R. § 121.201, NAICS code 513330 (changed to 517310 in October 2002).

<sup>47</sup> *Trends in Telephone Service* at Table 5.3.

<sup>48</sup> *Id.*

<sup>49</sup> 13 C.F.R. § 121.201, NAICS code 513310 (changed to 517110 in October 2002).

<sup>50</sup> *Trends in Telephone Service* at Table 5.3.

<sup>51</sup> *Id.*

<sup>52</sup> 13 C.F.R. § 121.201, NAICS code 513321 (changed to 517211 in October 2002).

<sup>53</sup> *Id.* § 121.201, NAICS code 513322 (changed to 517212 in October 2002).

<sup>54</sup> U.S. Census Bureau, 1997 Economic Census, Subject Series: Information, "Employment Size of Firms Subject to Federal Income Tax - 1997," Table 5, NAICS code 513321 (issued Oct. 2000).

employment of 999 or fewer employees, and an additional 17 firms had employment of 1,000 employees or more.<sup>55</sup> Thus, under this category and associated small business size standard, the majority of firms can be considered small. For the census category Cellular and Other Wireless Telecommunications firms, Census Bureau data for 1997 show that there were 977 firms in this category, total, that operated for the entire year.<sup>56</sup> Of this total, 965 firms had employment of 999 or fewer employees, and an additional 12 firms had employment of 1,000 employees or more.<sup>57</sup> Thus, under this second category and size standard, the majority of firms can, again, be considered small.

27 *Broadband Personal Communications Service.* The broadband Personal Communications Service (PCS) spectrum is divided into six frequency blocks designated A through F, and the Commission has held auctions for each block. The Commission defined "small entity" for Blocks C and F as an entity that has average gross revenues of \$40 million or less in the three previous calendar years.<sup>58</sup> For Block F, an additional classification for "very small business" was added and is defined as an entity that, together with its affiliates, has average gross revenues of not more than \$15 million for the preceding three calendar years.<sup>59</sup> These standards defining "small entity" in the context of broadband PCS auctions have been approved by the SBA.<sup>60</sup> No small businesses, within the SBA-approved small business size standards bid successfully for licenses in Blocks A and B. There were 90 winning bidders that qualified as small entities in the Block C auctions. A total of 93 small and very small business bidders won approximately 40 percent of the 1,479 licenses for Blocks D, E, and F.<sup>61</sup> On March 23, 1999, the Commission re-auctioned 347 C, D, E, and F Block licenses. There were 48 small business winning bidders. On January 26, 2001, the Commission completed the auction of 422 C and F Broadband PCS licenses in Auction No. 35. Of the 35 winning bidders in this auction, 29 qualified as "small" or "very small" businesses. Based on this information, the Commission concludes that the number of small broadband PCS licenses will include the 90 winning C Block bidders, the 93 qualifying bidders in the D, E, and F Block auctions, the 48 winning bidders in the 1999 re-auction, and the 29 winning bidders in the 2001 re-auction, for a total of 260 small entity broadband PCS providers, as defined by the SBA small business size standards and the Commission's auction rules. We note that, as a general matter, the number of winning bidders that qualify as small businesses at the close of an auction does not necessarily represent the number of small businesses currently in service. Also, the Commission does not generally track subsequent business size unless, in the context of assignments or transfers, unjust enrichment issues are implicated.

<sup>55</sup> *Id.* The census data do not provide a more precise estimate of the number of firms that have employment of 1,500 or fewer employees, the largest category provided is "Firms with 1,000 employees or more."

<sup>56</sup> U.S. Census Bureau, 1997 Economic Census, Subject Series Information, "Employment Size of Firms Subject to Federal Income Tax 1997," Table 5, NAICS code 513322 (issued Oct. 2000).

<sup>57</sup> *Id.* The census data do not provide a more precise estimate of the number of firms that have employment of 1,500 or fewer employees, the largest category provided is "Firms with 1,000 employees or more."

<sup>58</sup> See *Amendment of Parts 20 and 24 of the Commission's Rules – Broadband PCS Competitive Bidding and the Commercial Mobile Radio Service Spectrum Cap*, WT Docket No. 96-59, Report and Order, 61 FR 33859 (July 1, 1996), see also 47 C.F.R. § 24.720(b).

<sup>59</sup> See *id.*

<sup>60</sup> See e.g., *Implementation of Section 309(j) of the Communications Act – Competitive Bidding*, PP Docket No. 93-253, Fifth Report and Order, 59 FR 37566 (July 22, 1994).

<sup>61</sup> FCC News, Broadband PCS, D, E and F Block Auction Closes, No. 71744 (released January 14, 1997). See also *Amendment of the Commission's Rules Regarding Installment Payment Financing for Personal Communications Services (PCS) Licenses*, WT Docket No. 97-82, Second Report and Order, 62 FR 55348 (Oct. 24, 1997).

28. *Narrowband Personal Communications Services.* To date, two auctions of narrowband personal communications services (PCS) licenses have been conducted. For purposes of the two auctions that have already been held, “small businesses” were entities with average gross revenues for the prior three calendar years of \$40 million or less. Through these auctions, the Commission has awarded a total of 41 licenses, out of which 11 were obtained by small businesses. To ensure meaningful participation of small business entities in future auctions, the Commission has adopted a two-tiered small business size standard in the *Narrowband PCS Second Report and Order*.<sup>62</sup> A “small business” is an entity that, together with affiliates and controlling interests, has average gross revenues for the three preceding years of not more than \$40 million. A “very small business” is an entity that, together with affiliates and controlling interests, has average gross revenues for the three preceding years of not more than \$15 million. The SBA has approved these small business size standards.<sup>63</sup> In the future, the Commission will auction 459 licenses to serve Metropolitan Trading Areas (MTAs) and 408 response channel licenses. There is also one megahertz of narrowband PCS spectrum that has been held in reserve and that the Commission has not yet decided to release for licensing. The Commission cannot predict accurately the number of licenses that will be awarded to small entities in future actions. However, four of the 16 winning bidders in the two previous narrowband PCS auctions were small businesses, as that term was defined under the Commission’s Rules. The Commission assumes, for purposes of this analysis, that a large portion of the remaining narrowband PCS licenses will be awarded to small entities. The Commission also assumes that at least some small businesses will acquire narrowband PCS licenses by means of the Commission’s partitioning and disaggregation rules.

29. *220 MHz Radio Service – Phase I Licensees.* The 220 MHz service has both Phase I and Phase II licenses. Phase I licensing was conducted by lotteries in 1992 and 1993. There are approximately 1,515 such non-nationwide licensees and four nationwide licensees currently authorized to operate in the 220 MHz band. The Commission has not developed a small business size standard for small entities specifically applicable to such incumbent 220 MHz Phase I licensees. To estimate the number of such licensees that are small businesses, we apply the small business size standard under the SBA rules applicable to “Cellular and Other Wireless Telecommunications” companies. This standard provides that such a company is small if it employs no more than 1,500 persons.<sup>64</sup> According to Census Bureau data for 1997, there were 977 firms in this category, total, that operated for the entire year.<sup>65</sup> Of this total, 965 firms had employment of 999 or fewer employees, and an additional 12 firms had employment of 1,000 employees or more.<sup>66</sup> If this general ratio continues in the context of Phase I 220 MHz licensees, the Commission estimates that nearly all such licensees are small businesses under the SBA’s small business size standard.

30. *220 MHz Radio Service – Phase II Licensees.* The 220 MHz service has both Phase I and Phase II licenses. The Phase II 220 MHz service is a new service, and is subject to spectrum auctions. In the *220 MHz Third Report and Order*, we adopted a small business size standard for “small” and “very small” businesses for purposes of determining their eligibility for special provisions such as bidding.

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<sup>62</sup> *Amendment of the Commission’s Rules to Establish New Personal Communications Services, Narrowband PCS*, Docket No. ET 92-100, Docket No. PP 93-253, Second Report and Order and Second Further Notice of Proposed Rulemaking, 65 FR 35875 (June 6, 2000).

<sup>63</sup> See Letter to Amy Zoslov, Chief, Auctions and Industry Analysis Division, Wireless Telecommunications Bureau, FCC, from Aida Alvarez, Administrator, SBA (Dec. 2, 1998).

<sup>64</sup> 13 C.F.R. § 121.201, NAICS code 513322 (changed to 517212 in October 2002).

<sup>65</sup> U.S. Census Bureau, 1997 Economic Census, Subject Series. Information, “Employment Size of Firms Subject to Federal Income Tax. 1997,” Table 5, NAICS code 513322 (issued Oct. 2000).

<sup>66</sup> *Id.* The census data do not provide a more precise estimate of the number of firms that have employment of 1,500 or fewer employees, the largest category provided is “Firms with 1,000 employees or more.”

credits and installment payments.<sup>67</sup> This small business size standard indicates that a "small business" is an entity that, together with its affiliates and controlling principals, has average gross revenues not exceeding \$15 million for the preceding three years.<sup>68</sup> A "very small business" is an entity that, together with its affiliates and controlling principals, has average gross revenues that do not exceed \$3 million for the preceding three years. The SBA has approved these small business size standards.<sup>69</sup> Auctions of Phase II licenses commenced on September 15, 1998, and closed on October 22, 1998.<sup>70</sup> In the first auction, 908 licenses were auctioned in three different-sized geographic areas: three nationwide licenses, 30 Regional Economic Area Group (EAG) Licenses, and 875 Economic Area (EA) Licenses. Of the 908 licenses auctioned, 693 were sold. Thirty-nine small businesses won licenses in the first 220 MHz auction. The second auction included 225 licenses: 216 EA licenses and 9 EAG licenses. Fourteen companies claiming small business status won 158 licenses.<sup>71</sup>

31 *800 MHz and 900 MHz Specialized Mobile Radio Licenses* The Commission awards "small entity" and "very small entity" bidding credits in auctions for Specialized Mobile Radio (SMR) geographic area licenses in the 900 MHz bands to firms that had revenues of no more than \$15 million in each of the three previous calendar years, or that had revenues of no more than \$3 million in each of the previous calendar years.<sup>72</sup> The SBA has approved these size standards.<sup>73</sup> The Commission awards "small entity" and "very small entity" bidding credits in auctions for Specialized Mobile Radio (SMR) geographic area licenses in the 800 MHz bands to firms that had revenues of no more than \$40 million in each of the three previous calendar years, or that had revenues of no more than \$15 million in each of the previous calendar years.<sup>74</sup> These bidding credits apply to SMR providers in the 800 MHz and 900 MHz bands that either hold geographic area licenses or have obtained extended implementation authorizations. The Commission does not know how many firms provide 800 MHz or 900 MHz geographic area SMR service pursuant to extended implementation authorizations, nor how many of these providers have annual revenues of no more than \$15 million. One firm has over \$15 million in revenues. The Commission assumes, for purposes here, that all of the remaining existing extended implementation authorizations are held by small entities, as that term is defined by the SBA. The Commission has held auctions for geographic area licenses in the 800 MHz and 900 MHz SMR bands. There were 60 winning bidders that qualified as small or very small entities in the 900 MHz SMR auctions. Of the 1,020 licenses won in the 900 MHz auction, bidders qualifying as small or very small entities won 263 licenses. In the 800 MHz auction, 38 of the 524 licenses won were won by small and very small entities. We note that, as a general matter, the number of winning bidders that qualify as small businesses at the close of an auction

<sup>67</sup> *Amendment of Part 90 of the Commission's Rules to Provide for the Use of the 220-222 MHz Band by the Private Land Mobile Radio Service*, PR Docket No. 89-552, GN Docket No. 93-252, PP Docket No. 93-253, Third Report and Order and Fifth Notice of Proposed Rulemaking, 12 FCC Rcd 10943, 11068-70, at paras. 291-95 (1997) (220 MHz Third Report and Order).

<sup>68</sup> *Id.* at 11068-70, para. 291.

<sup>69</sup> See letter to D. Phythyon, Chief, Wireless Telecommunications Bureau, FCC, from Aida Alvarez, Administrator, SBA (Jan. 6, 1998).

<sup>70</sup> See generally Public Notice, "220 MHz Service Auction Closes," 14 FCC Rcd 605 (1998).

<sup>71</sup> Public Notice, "Phase II 220 MHz Service Spectrum Auction Closes," 14 FCC Rcd 11218 (1999).

<sup>72</sup> 47 C.F.R. § 90.814(b)(1).

<sup>73</sup> See Letter from Aida Alvarez, Administration, Small Business Administration to Daniel B. Phythyon, Chief, Wireless Telecommunications Bureau, Federal Communications Commission (Oct. 27, 1997). See Letter from Aida Alvarez, Administrator, Small Business Administration to Thomas Sugrue, Chief, Auctions and Industry Analysis Division, Wireless Telecommunications Bureau, Federal Communications Commission (Aug. 10, 1999).

<sup>74</sup> 47 C.F.R. § 90.814(b)(1). A request for approval of 800 MHz standards was sent to the SBA on May 13, 1999. The matter remains pending.

does not necessarily represent the number of small businesses currently in service. Also, the Commission does not generally track subsequent business size unless, in the context of assignments or transfers, unjust enrichment issues are implicated

32 *Paging* In the *Paging Third Report and Order*, we developed a small business size standard for “small businesses” and “very small businesses” for purposes of determining their eligibility for special provisions such as bidding credits and installment payments.<sup>75</sup> A “small business” is an entity that, together with its affiliates and controlling principals, has average gross revenues not exceeding \$15 million for the preceding three years. Additionally, a “very small business” is an entity that, together with its affiliates and controlling principals, has average gross revenues that are not more than \$3 million for the preceding three years. The SBA has approved these size standards.<sup>76</sup> An auction of Metropolitan Economic Area licenses commenced on February 24, 2000, and closed on March 2, 2000.<sup>77</sup> Of the 985 licenses auctioned, 440 were sold. Fifty-seven companies claiming small business status won. At present, there are approximately 24,000 Private-Paging site-specific licenses and 74,000 Common Carrier Paging licenses. According to the most recent *Trends in Telephone Service*, 471 carriers reported that they were engaged in the provision of either paging and messaging services or other mobile services.<sup>78</sup> Of those, the Commission estimates that 450 are small, under the SBA business size standard specifying that firms are small if they have 1,500 or fewer employees.<sup>79</sup>

33 *700 MHz Guard Band Licensees* In the 700 MHz Guard Band Order, we adopted a small business size standard for “small businesses” and “very small businesses” for purposes of determining their eligibility for special provisions such as bidding credits and installment payments.<sup>80</sup> A “small business” as an entity that, together with its affiliates and controlling principals, has average gross revenues not exceeding \$15 million for the preceding three years. Additionally, a “very small business” is an entity that, together with its affiliates and controlling principals, has average gross revenues that are not more than \$3 million for the preceding three years. An auction of 52 Major Economic Area (MEA) licenses commenced on September 6, 2000, and closed on September 21, 2000.<sup>81</sup> Of the 104 licenses auctioned, 96 licenses were sold to nine bidders. Five of these bidders were small businesses that won a total of 26 licenses. A second auction of 700 MHz Guard Band licenses commenced on February 13, 2001 and closed on February 21, 2001. All eight of the licenses auctioned were sold to three bidders. One of these bidders was a small business that won a total of two licenses.<sup>82</sup>

<sup>75</sup> *220 MHz Third Report and Order*, 12 FCC Rcd at 11068-70, paras. 291-295, 62 FR 16004 at paras. 291-295 (1997).

<sup>76</sup> See Letter from Aida Alvarez, Administrator, Small Business Administration to Thomas Sugrue, Chief, Auctions and Industry Analysis Division, Wireless Telecommunications Bureau, Federal Communications Commission (June 4, 1999).

<sup>77</sup> *Revision of Part 22 and Part 90 of the Commission's Rules to Facilitate Future Development of Paging Systems*, WT Docket No. 96-18, PR Docket No. 93-253, Memorandum Opinion and Order on Reconsideration and Third Report and Order, 14 FCC Rcd 10030, 10085, at para. 98 (1999).

<sup>78</sup> *Trends in Telephone Service* at Table 5.3.

<sup>79</sup> *Id.* The SBA size standard is that of Paging, 13 C.F.R. § 121.201, NAICS code 517211.

<sup>80</sup> See *Service Rules for the 746-764 MHz Bands, and Revisions to part 27 of the Commission's Rules*, WT Docket No. 99-168, Second Report and Order, 15 FCC Rcd 5299, 5344, at para. 108 (2000).

<sup>81</sup> See generally Public Notice, “220 MHz Service Auction Closes,” Report No. WT 98-36 (Wireless Telecommunications Bureau, Oct. 23, 1998).

<sup>82</sup> Public Notice, “700 MHz Guard Band Auction Closes,” DA 01-478 (released Feb. 22, 2001).

34. *Rural Radiotelephone Service* The Commission has not adopted a size standard for small businesses specific to the Rural Radiotelephone Service.<sup>83</sup> A significant subset of the Rural Radiotelephone Service is the Basic Exchange Telephone Radio System (BETRS).<sup>84</sup> The Commission uses the SBA's small business size standard applicable to "Cellular and Other Wireless Telecommunications," i.e., an entity employing no more than 1,500 persons.<sup>85</sup> There are approximately 1,000 licensees in the Rural Radiotelephone Service, and the Commission estimates that there are 1,000 or fewer small entity licensees in the Rural Radiotelephone Service that may be affected by the rules and policies adopted herein.

35. *Air-Ground Radiotelephone Service* The Commission has not adopted a small business size standard specific to the Air-Ground Radiotelephone Service.<sup>86</sup> We will use SBA's small business size standard applicable to "Cellular and Other Wireless Telecommunications," i.e., an entity employing no more than 1,500 persons.<sup>87</sup> There are approximately 100 licensees in the Air-Ground Radiotelephone Service, and we estimate that almost all of them qualify as small under the SBA small business size standard.

36. *Aviation and Marine Radio Services* Small businesses in the aviation and marine radio services use a very high frequency (VHF) marine or aircraft radio and, as appropriate, an emergency position-indicating radio beacon (and/or radar) or an emergency locator transmitter. The Commission has not developed a small business size standard specifically applicable to these small businesses. For purposes of this analysis, the Commission uses the SBA small business size standard for the category "Cellular and Other Telecommunications," which is 1,500 or fewer employees.<sup>88</sup> Most applicants for recreational licenses are individuals. Approximately 581,000 ship station licensees and 131,000 aircraft station licensees operate domestically and are not subject to the radio carriage requirements of any statute or treaty. For purposes of our evaluations in this analysis, we estimate that there are up to approximately 712,000 licensees that are small businesses (or individuals) under the SBA standard. In addition, between December 3, 1998 and December 14, 1998, the Commission held an auction of 42 VHF Public Coast licenses in the 157.1875-157.4500 MHz (ship transmit) and 161.775-162.0125 MHz (coast transmit) bands. For purposes of the auction, the Commission defined a "small" business as an entity that, together with controlling interests and affiliates, has average gross revenues for the preceding three years not to exceed \$15 million dollars. In addition, a "very small" business is one that, together with controlling interests and affiliates, has average gross revenues for the preceding three years not to exceed \$3 million dollars.<sup>89</sup> There are approximately 10,672 licensees in the Marine Coast Service, and the Commission estimates that almost all of them qualify as "small" businesses under the above special small business size standards.

37. *Fixed Microwave Services* Fixed microwave services include common carrier,<sup>90</sup> private operational-fixed,<sup>91</sup> and broadcast auxiliary radio services.<sup>92</sup> At present, there are approximately 22,015

<sup>83</sup> The service is defined in § 22.99 of the Commission's Rules, 47 C.F.R. § 22.99.

<sup>84</sup> BETRS is defined in §§ 22.757 and 22.759 of the Commission's Rules, 47 C.F.R. §§ 22.757 and 22.759.

<sup>85</sup> 13 C.F.R. § 121.201, NAICS code 513322 (changed to 517212 in October 2002).

<sup>86</sup> The service is defined in § 22.99 of the Commission's Rules, 47 C.F.R. § 22.99.

<sup>87</sup> 13 C.F.R. § 121.201, NAICS codes 513322 (changed to 517212 in October 2002).

<sup>88</sup> *Id.* § 121.201, NAICS code 513322 (changed to 517212 in October 2002).

<sup>89</sup> *Amendment of the Commission's Rules Concerning Maritime Communications*, PR Docket No. 92-257, Third Report and Order and Memorandum Opinion and Order, 13 FCC Rcd 19853 (1998).

<sup>90</sup> See 47 C.F.R. §§ 101 *et seq.* (formerly, Part 21 of the Commission's Rules) for common carrier fixed microwave services (except Multipoint Distribution Service).

common carrier fixed licensees and 61,670 private operational-fixed licensees and broadcast auxiliary radio licensees in the microwave services. The Commission has not created a size standard for a small business specifically with respect to fixed microwave services. For purposes of this analysis, the Commission uses the SBA small business size standard for the category "Cellular and Other Telecommunications," which is 1,500 or fewer employees.<sup>93</sup> The Commission does not have data specifying the number of these licensees that have more than 1,500 employees, and thus are unable at this time to estimate with greater precision the number of fixed microwave service licensees that would qualify as small business concerns under the SBA's small business size standard. Consequently, the Commission estimates that there are up to 22,015 common carrier fixed licensees and up to 61,670 private operational-fixed licensees and broadcast auxiliary radio licensees in the microwave services that may be small and may be affected by the rules and policies adopted herein. We noted, however, that the common carrier microwave fixed licensee category includes some large entities.

38. *Offshore Radiotelephone Service* This service operates on several UHF television broadcast channels that are not used for television broadcasting in the coastal areas of states bordering the Gulf of Mexico.<sup>94</sup> There are presently approximately 55 licensees in this service. We are unable to estimate at this time the number of licensees that would qualify as small under the SBA's small business size standard for "Cellular and Other Wireless Telecommunications" services.<sup>95</sup> Under that SBA small business size standard, a business is small if it has 1,500 or fewer employees.<sup>96</sup>

39. *Wireless Communications Services* This service can be used for fixed, mobile, radiolocation, and digital audio broadcasting satellite uses. The Commission established small business size standards for the wireless communications services (WCS) auction. A "small business" is an entity with average gross revenues of \$40 million for each of the three preceding years, and a "very small business" is an entity with average gross revenues of \$15 million for each of the three preceding years. The SBA has approved these small business size standards.<sup>97</sup> The Commission auctioned geographic area licenses in the WCS service. In the auction, there were seven winning bidders that qualified as "very small business" entities, and one that qualified as a "small business" entity. We conclude that the number of geographic area WCS licensees affected by this analysis includes these eight entities.

40. *39 GHz Service* The Commission created a special small business size standard for 39 GHz licenses – an entity that has average gross revenues of \$40 million or less in the three previous

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<sup>91</sup> Persons eligible under parts 80 and 90 of the Commission's Rules can use Private Operational-Fixed Microwave services. See 47 C.F.R. Parts 80 and 90. Stations in this service are called operational-fixed to distinguish them from common carrier and public fixed stations. Only the licensee may use the operational-fixed station, and only for communications related to the licensee's commercial, industrial, or safety operations.

<sup>92</sup> Auxiliary Microwave Service is governed by Part 74 of Title 47 of the Commission's Rules. See 47 C.F.R. Part 74. This service is available to licensees of broadcast stations and to broadcast and cable network entities. Broadcast auxiliary microwave stations are used for relaying broadcast television signals from the studio to the transmitter, or between two points such as a main studio and an auxiliary studio. The service also includes mobile television pickups, which relay signals from a remote location back to the studio.

<sup>93</sup> 13 C.F.R. § 121.201, NAICS code 513322 (changed to 517212 in October 2002).

<sup>94</sup> This service is governed by Subpart I of Part 22 of the Commission's Rules. See 47 C.F.R. §§ 22.1001-22.1037.

<sup>95</sup> 13 C.F.R. § 121.201, NAICS code 513322 (changed to 517212 in October 2002).

<sup>96</sup> *Id.*

<sup>97</sup> See Letter to Amy Zoslov, Chief, Auctions and Industry Analysis Division, Wireless Telecommunications Bureau, FCC, from Aida Alvarez, Administrator, SBA (Dec. 2, 1998).

calendar years.<sup>98</sup> An additional size standard for “very small business” is: an entity that, together with affiliates, has average gross revenues of not more than \$15 million for the preceding three calendar years.<sup>99</sup> The SBA has approved these small business size standards.<sup>100</sup> The auction of the 2,173 39 GHz licenses began on April 12, 2000 and closed on May 8, 2000. The 18 bidders who claimed small business status won 849 licenses. Consequently, the Commission estimates that 18 or fewer 39 GHz licensees are small entities that may be affected by the rules and policies adopted herein.

41 *Multipoint Distribution Service, Multichannel Multipoint Distribution Service, and ITFS* Multichannel Multipoint Distribution Service (MMDS) systems, often referred to as “wireless cable,” transmit video programming to subscribers using the microwave frequencies of the Multipoint Distribution Service (MDS) and Instructional Television Fixed Service (ITFS).<sup>101</sup> In connection with the 1996 MDS auction, the Commission established a small business size standard as an entity that had annual average gross revenues of less than \$40 million in the previous three calendar years.<sup>102</sup> The MDS auctions resulted in 67 successful bidders obtaining licensing opportunities for 493 Basic Trading Areas (BTAs). Of the 67 auction winners, 61 met the definition of a small business. MDS also includes licensees of stations authorized prior to the auction. In addition, the SBA has developed a small business size standard for Cable and Other Program Distribution, which includes all such companies generating \$12.5 million or less in annual receipts.<sup>103</sup> According to Census Bureau data for 1997, there were a total of 1,311 firms in this category, total, that had operated for the entire year.<sup>104</sup> Of this total, 1,180 firms had annual receipts of under \$10 million and an additional 52 firms had receipts of \$10 million or more but less than \$25 million. Consequently, we estimate that the majority of providers in this service category are small businesses that may be affected by the rules and policies adopted herein. This SBA small business size standard also appears applicable to ITFS. There are presently 2,032 ITFS licensees. All but 100 of these licenses are held by educational institutions. Educational institutions are included in this analysis as small entities.<sup>105</sup> Thus, we tentatively conclude that at least 1,932 licensees are small businesses.

42 *Local Multipoint Distribution Service.* Local Multipoint Distribution Service (LMDS) is a fixed broadband point-to-multipoint microwave service that provides for two-way video telecommunications.<sup>106</sup> The auction of the 1,030 Local Multipoint Distribution Service (LMDS) licenses

<sup>98</sup> See Amendment of the Commission’s Rules Regarding the 37.0-38.6 GHz and 38.6-40.0 GHz Bands, ET Docket No. 95-183, *Report and Order*, 63 FR 6079 (Feb. 6, 1998).

<sup>99</sup> *Id.*

<sup>100</sup> See Letter to Kathleen O’Brien Ham, Chief, Auctions and Industry Analysis Division, Wireless Telecommunications Bureau, FCC, from Aida Alvarez, Administrator, SBA (Feb. 4, 1998).

<sup>101</sup> *Amendment of Parts 21 and 74 of the Commission’s Rules with Regard to Filing Procedures in the Multipoint Distribution Service and in the Instructional Television Fixed Service and Implementation of Section 309(j) of the Communications Act – Competitive Bidding*, MM Docket No. 94-131 and PP Docket No. 93-253, *Report and Order*, 10 FCC Rcd 9589, 9593 at para. 7 (1995).

<sup>102</sup> 47 C.F.R. § 21.961(b)(1).

<sup>103</sup> 13 C.F.R. § 121.201, NAICS code 513220 (changed to 517510 in October 2002).

<sup>104</sup> U.S. Census Bureau, 1997 Economic Census, Subject Series Information, “Establishment and Firm Size (Including Legal Form of Organization),” Table 4, NAICS code 513220 (issued October 2000).

<sup>105</sup> In addition, the term “small entity” within SBREFA applies to small organizations (nonprofits) and to small governmental jurisdictions (cities, counties, towns, townships, villages, school districts, and special districts with populations of less than 50,000). 5 U.S.C. §§ 601(4)-(6). We do not collect annual revenue data on ITFS licensees.

<sup>106</sup> See *Rulemaking to Amend Parts 1, 2, 21, and 25 of the Commission’s Rules to Redesignate the 27.5-29.5 GHz Frequency Band, to Reallocate the 29.5-30.0 GHz Frequency Band, and to Establish Rules and Policies for Local*

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began on February 18, 1998 and closed on March 25, 1998. The Commission established a small business size standard for LMDS licenses as an entity that has average gross revenues of less than \$40 million in the three previous calendar years<sup>107</sup>. An additional small business size standard for "very small business" was added as an entity that, together with its affiliates, has average gross revenues of not more than \$15 million for the preceding three calendar years<sup>108</sup>. The SBA has approved these small business size standards in the context of LMDS auctions<sup>109</sup>. There were 93 winning bidders that qualified as small entities in the LMDS auctions. A total of 93 small and very small business bidders won approximately 277 A Block licenses and 387 B Block licenses. On March 27, 1999, the Commission re-auctioned 161 licenses, there were 40 winning bidders. Based on this information, we conclude that the number of small LMDS licenses consists of the 93 winning bidders in the first auction and the 40 winning bidders in the re-auction, for a total of 133 small entity LMDS providers.

43 *218-219 MHz Service* The first auction of 218-219 MHz spectrum resulted in 170 entities winning licenses for 594 Metropolitan Statistical Area (MSA) licenses. Of the 594 licenses, 557 were won by entities qualifying as a small business. For that auction, the small business size standard was an entity that, together with its affiliates, has no more than a \$6 million net worth and, after federal income taxes (excluding any carry over losses), has no more than \$2 million in annual profits each year for the previous two years<sup>110</sup>. In the *218-219 MHz Report and Order and Memorandum Opinion and Order*, we established a small business size standard for a "small business" as an entity that, together with its affiliates and persons or entities that hold interests in such an entity and their affiliates, has average annual gross revenues not to exceed \$15 million for the preceding three years.<sup>111</sup> A "very small business" is defined as an entity that, together with its affiliates and persons or entities that hold interests in such an entity and its affiliates, has average annual gross revenues not to exceed \$3 million for the preceding three years<sup>112</sup>. The SBA has approved these size standards.<sup>113</sup> We cannot estimate, however, the number of licenses that will be won by entities qualifying as small or very small businesses under our rules in future auctions of 218-219 MHz spectrum.

44 *24 GHz – Incumbent Licensees* This analysis may affect incumbent licensees who were relocated to the 24 GHz band from the 18 GHz band, and applicants who wish to provide services in the 24 GHz band. The applicable SBA small business size standard is that of "Cellular and Other Wireless Telecommunications" companies. This category provides that such a company is small if it employs no more than 1,500 persons<sup>114</sup>. According to Census Bureau data for 1997, there were 977 firms in this

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*Multipoint Distribution Service and for Fixed Satellite Services*, CC Docket No. 92-297, Second Report and Order, 12 FCC Rcd 12545 (1997).

<sup>107</sup> *Id*

<sup>108</sup> *See id*

<sup>109</sup> *See* Letter to Dan Phythyon, Chief, Wireless Telecommunications Bureau, FCC, from Aida Alvarez, Administrator, SBA (Jan. 6, 1998).

<sup>110</sup> *Implementation of Section 309(j) of the Communications Act – Competitive Bidding*, PP Docket No. 93-253, Fourth Report and Order, 59 FR 24947 (May 13, 1994).

<sup>111</sup> *Amendment of Part 95 of the Commission's Rules to Provide Regulatory Flexibility in the 218-219 MHz Service*, WT Docket No. 98-169, Report and Order and Memorandum Opinion and Order, 64 FR 59656 (Nov. 3, 1999).

<sup>112</sup> *Id*

<sup>113</sup> *See* Letter to Daniel B. Phythyon, Chief, Wireless Telecommunications Bureau, Federal Communications Commission, from Aida Alvarez, Administrator, Small Business Administration (Jan. 6, 1998).

<sup>114</sup> 13 C.F.R. § 121.201, NAICS code 513322 (changed to 517212 in October 2002).

category, total, that operated for the entire year<sup>115</sup> Of this total, 965 firms had employment of 999 or fewer employees, and an additional 12 firms had employment of 1,000 employees or more.<sup>116</sup> Thus, under this size standard, the great majority of firms can be considered small. These broader census data notwithstanding, we believe that there are only two licensees in the 24 GHz band that were relocated from the 18 GHz band, Teligent<sup>117</sup> and TRW, Inc. It is our understanding that Teligent and its related companies have less than 1,500 employees, though this may change in the future. TRW is not a small entity. Thus, only one incumbent licensee in the 24 GHz band is a small business entity.

45. *24 GHz – Future Licensees.* With respect to new applicants in the 24 GHz band, the small business size standard for “small business” is an entity that, together with controlling interests and affiliates, has average annual gross revenues for the three preceding years not in excess of \$15 million.<sup>118</sup> “Very small business” in the 24 GHz band is an entity that, together with controlling interests and affiliates, has average gross revenues not exceeding \$3 million for the preceding three years.<sup>119</sup> The SBA has approved these small business size standards.<sup>120</sup> These size standards will apply to the future auction, if held.

46. *Internet Service Providers.* While internet service providers (ISPs) are only indirectly affected by our present actions, and ISPs are therefore not formally included within this present IRFA, we address them here informally to create a fuller record and to recognize their participation in this proceeding. The SBA has developed a small business size standard for Online Information Services, which consists of all such companies having \$21 million or less in annual receipts.<sup>121</sup> According to Census Bureau data for 1997, there were 2,751 firms in this category, total, that operated for the entire year.<sup>122</sup> Of this total, 2,659 firms had annual receipts of \$9,999,999 or less, and an additional 67 had receipts of \$10 million to \$24,999,999.<sup>123</sup> Thus, under this size standard, the majority of firms can be considered small.

#### **4. Description of Projected Reporting, Recordkeeping, and Other Compliance Requirements**

47. The Notice seeks comment on the Joint Conference Recommendation while also seeking comment from parties proposing alternative requirements for regulatory accounting and related reporting. Apart from the future, indeterminate alternative proposals, this IRFA can project the reporting,

<sup>115</sup> U.S. Census Bureau, 1997 Economic Census, Subject Series Information, “Employment Size of Firms Subject to Federal Income Tax – 1997,” Table 5, NAICS code 513322 (issued Oct. 2000).

<sup>116</sup> *Id.* The census data do not provide a more precise estimate of the number of firms that have employment of 1,500 or fewer employees, the largest category provided is “Firms with 1,000 employees or more.”

<sup>117</sup> Teligent acquired the DEMS licenses of FirstMark, the only licensee other than TRW in the 24 GHz band whose license has been modified to require relocation to the 24 GHz band.

<sup>118</sup> *Amendments to Parts 1, 2, 87 and 101 of the Commission’s Rules to License Fixed Services at 24 GHz*, WT Docket No. 99-327, Report and Order, 15 FCC Rcd 16934, 16967 (2000), *see also* 47 C.F.R. § 101.538(a)(2).

<sup>119</sup> *Amendments to Parts 1, 2, 87 and 101 of the Commission’s Rules to License Fixed Services at 24 GHz*, WT Docket No. 99-327, Report and Order, 15 FCC Rcd at 16967, *see also* 47 C.F.R. § 101.538(a)(1).

<sup>120</sup> *See* Letter to Margaret W. Wiener, Deputy Chief, Auctions and Industry Analysis Division, Wireless Telecommunications Bureau, FCC, from Gary M. Jackson, Assistant Administrator, SBA (July 28, 2000).

<sup>121</sup> 13 C.F.R. § 121.201, NAICS code 514191 (changed to 518111 in October 2002).

<sup>122</sup> U.S. Census Bureau, 1997 Economic Census, Subject Series Information, “Receipts Size of Firms Subject to Federal Income Tax – 1997,” Table 4, NAICS code 514191 (issued October 2000).

<sup>123</sup> *Id.*

recordkeeping and other compliance requirements of the existing proposed Joint Conference Recommendation. The Joint Conference's recommendations to reinstate certain Part 32 Accounts, if adopted, would not impose any additional burden on ILECs because the Commission's prior action to aggregate the accounts has been suspended. However, the Joint Conference's recommendation to add several separate accounts to the Commission's Part 32 rules, if adopted, would impose additional reporting obligations according to the terms of each account. Furthermore, the Joint Conference's recommendations concerning affiliate transactions requirements, if adopted, generally would impose additional burdens due to new regulatory and related reporting requirements, together with broader applicability. Finally, the Joint Conference's recommendation to reinstate the sheath kilometer reporting requirement for ARMIS would impose an increased burden on ILECs, if the Commission were to require ARMIS reporting of local loop facilities as loop sheath kilometers.

## 5. Steps Taken to Minimize Significant Economic Impact on Small Entities, and Significant Alternatives Considered

48 The RFA requires an agency to describe any significant alternatives that it has considered in reaching its proposed approach, which may include the following four alternatives (among others): (1) the establishment of differing compliance or reporting requirements or timetables that take into account the resources available to small entities, (2) the clarification, consolidation, or simplification of compliance or reporting requirements under the rule for small entities, (3) the use of performance, rather than design, standards, and (4) an exemption from coverage of the rule, or any part thereof, for small entities.<sup>124</sup>

49. As described in Section 1 of this IRFA, the Joint Conference's recommended modifications to Part 32 do not apply to Class B accounts, which include all carriers with indexed revenue thresholds below \$121 million, and those carriers with thresholds between \$121 million and \$7.083 billion that elect to maintain accounts at the Class B level. For the purposes of this IRFA, we shall assume that many small entities fall within the Class B account classification, and therefore are not subject to the proposed changes to Part 32. We note that small entities with indexed revenue thresholds of at least \$121 million always may elect to maintain accounts at the Class B level.<sup>125</sup> Under this option, the Commission minimizes any possible significant economic impact on small entities with respect to modifying the accounting and related reporting burdens in Part 32.

50 The Joint Conference's recommendations on affiliate transactions requirements generally propose greater burdens on Class B carriers, including small entities. For example, the recommendation to apply the affiliate transactions rules to transactions between incumbent LECs within the same holding company would add a burden from which carriers currently are exempt. The Joint Conference's recommendations on ARMIS reporting, however, do not apply to Class B carriers, and for the reasons discussed above, this Class B exemption serves to minimize the burdens on small entities. Furthermore, the recommendation not to distinguish between dominant and non-dominant ILECs under the Commission's accounting and reporting rules imposes no impact on small entities. We encourage small entities to comment on our proposals and to suggest any other appropriate alternatives.

## 6. Federal Rules that May Duplicate, Overlap, or Conflict with the Proposed Rules

51 None.

<sup>124</sup> 5 U.S.C. § 603(c)(1)-(c)(4)

<sup>125</sup> For the purposes of this IRFA, we shall also assume that no small entity exceeds the non-discretionary, Class A indexed revenue threshold of \$7.083 billion.

**B. Ex Parte Presentations**

52. This proceeding shall be governed by "permit-but-disclose" *ex parte* procedures that are applicable to non-restricted proceedings under 47 C.F.R. § 1.1206. Parties making oral *ex parte* presentations are reminded that memoranda summarizing the presentation must contain a summary of the substance of the presentation and not merely a listing of the subjects discussed. More than a one- or two-sentence description of the views and arguments presented generally is required. See 47 C.F.R. § 1.1206(b)(2). Other rules pertaining to oral and written presentations are set forth in section 1.1206(b) as well.

**C. Comment Filing Procedures**

53. Pursuant to sections 1.415 and 1.419 of the Commission's rules, 47 C.F.R. §§ 1.415, 1.419, interested parties may file comments on or before 30 days after publication of this Notice in the Federal Register, and reply comments on or before 45 days after publication of this Notice in the Federal Register. All comments and reply comments should reference the docket numbers of this proceeding, WC Docket No. 02-269 and CC Docket Nos. 00-199, 80-286, 99-301. Comments may be filed using the Commission's Electronic Comment Filing System (ECFS), or by filing paper copies.<sup>126</sup>

54. Parties filing paper copies must file an original and four copies of each filing. Since multiple docket or rulemaking numbers appear in the caption of this proceeding, commenters must submit two additional copies for each additional docket or rulemaking number. All filings must be addressed to Marlene H. Dortch, Secretary, Federal Communications Commission. Filings can be sent by hand or messenger delivery, by commercial overnight courier, or by first-class or overnight U.S. Postal Service mail (although we continue to experience delays in receiving U.S. Postal Service mail). The Commission's contractor, Natek, Inc., will receive hand-delivered or messenger-delivered paper filings for the Commission's Secretary at 236 Massachusetts Avenue, N.E., Suite 110, Washington, D.C. 20002. The filing hours at this location are 8:00 a.m. to 7:00 p.m. All hand deliveries must be held together with rubber bands or fasteners. Any envelopes must be disposed of before entering the building. Commercial overnight mail (other than U.S. Postal Service Express Mail and Priority Mail) must be sent to 9300 East Hampton Drive, Capitol Heights, MD 20743. U.S. Postal Service first-class mail, Express Mail, and Priority Mail should be addressed to 445 12th Street, S.W., Washington, DC 20554.

55. Comments filed through the ECFS can be sent via the Internet at <http://www.fcc.gov/cgb/ecfs>. Since multiple docket or rulemaking numbers appear in the caption of this proceeding, commenters must transmit one electronic copy for each docket or rulemaking number referenced in the caption. In completing the transmittal screen, commenters should include their full name, Postal Service mailing address, and WC Docket No. 02-269 and CC Docket Nos. 00-199, 80-286, 99-301. Parties may also submit an electronic copy by Internet e-mail. To get filing instructions for e-mail comments, commenters should send an e-mail to [ecfs@fcc.gov](mailto:ecfs@fcc.gov), and should include the following words in the body of the message: "get form <your e-mail address>." A sample form and directions will be sent in reply. Commenters also may obtain a copy of the ASCII Electronic Transmittal Form (FORM-ET) at <http://www.fcc.gov/cgb/ecfs/email.html>.

56. Regardless of whether parties choose to file electronically or by paper, parties should also file one copy of any document filed in this docket with the Commission's copy contractor, Qualex International, Portals II, 445 12th Street, S.W., Washington, DC 20554 (telephone 202-863-2893,

<sup>126</sup> See *Electronic Filing of Documents in Rulemaking Proceedings*, GC Docket No. 97-113, Report and Order, 13 FCC Rcd 11322, 11326 para. 8 (1998).

facsimile 202-863-2898) or via e-mail to [qualexint@aol.com](mailto:qualexint@aol.com). In addition, one copy of each submission must be sent to the Chief, Pricing Policy Division, 445 12th Street, S.W., Washington, DC 20554

57 Documents filed in this proceeding will be available for public inspection during regular business hours in the Commission's Reference Information Center, 445 12th Street, S.W., Washington, DC 20554, and will be placed on the Commission's Internet site. They may also be purchased from the Commission's duplicating contractor, Qualex International, Portals II, 445 12th Street, S.W., Room CY-B402, Washington, DC 20554, telephone 202-863-2893, facsimile 202-863-2898, e-mail [qualexint@aol.com](mailto:qualexint@aol.com).

58. Accessible formats (computer diskettes, large print, audio recording and Braille) are available to persons with disabilities by contacting the Consumer & Governmental Affairs Bureau at (202) 418-0531, TTY (202) 418-7365, or [fcc504@fcc.gov](mailto:fcc504@fcc.gov)

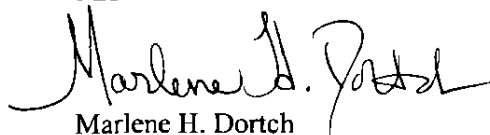
59 Written comments by the public on the proposed and/or modified information collections are due on the same day as comments on the Notice, *i.e.*, on or before 30 days after publication of the Notice in the Federal Register. Written comments must be submitted by OMB on the proposed and/or modified information collections on or before 30 days after publication of the Notice in the Federal Register. In addition to filing comments with the Secretary, a copy of any comments on the information collections contained herein should be submitted to Judith B. Herman, Federal Communications Commission, 445 12th Street, S.W., Washington, DC 20554, or via the Internet to [jbherman@fcc.gov](mailto:jbherman@fcc.gov), and to Jeanette Thornton, OMB Desk Officer, Room 10236 NEOB, 725 17th Street, N.W., Washington, DC 20503, or via the Internet to [JThornton@omb.eop.gov](mailto:JThornton@omb.eop.gov)

#### IV. ORDERING CLAUSES

60 Accordingly, IT IS ORDERED, pursuant to the authority contained in sections 1, 4(i), 4(j), 201-205, 219, 220, 251, 252 and 303 of the Communications Act of 1934, as amended, 47 U.S.C §§ 151, 154(i), (j), 201-205, 251, 252 and 303, that NOTICE IS HEREBY GIVEN of the rulemaking described above and COMMENT IS SOUGHT on those issues.

61 IT IS FURTHER ORDERED that the Commission's Consumer Information Bureau, Reference Information Center, SHALL SEND a copy of this Notice of Proposed Rulemaking, including the Initial Regulatory Flexibility Analysis, to the Chief Counsel for Advocacy of the Small Business Administration

FEDERAL COMMUNICATIONS COMMISSION

  
Marlene H. Dortch  
Secretary

**APPENDIX A**

**JOINT CONFERENCE RECOMMENDATION**



Federal Communications Commission  
Washington, D.C. 20554

October 9, 2003

Marlene H. Dortch  
Secretary  
Federal Communications Commission  
445 12<sup>th</sup> Street, S.W.  
Washington, DC 20554

Re: Federal-State Joint Conference on Accounting Issues, WC Docket 02-269

Dear Ms. Dortch:

By this letter, the Federal-State Joint Conference on Accounting Issues (Joint Conference) transmits a report detailing a series of proposed recommendations to the Commission's accounting requirements. Pursuant to section 410(b) of the Communications Act of 1934, as amended (the Act), the Commission convened the Federal-State Joint Conference on Accounting Issues "to provide a forum for an ongoing dialogue between the Commission and the states in order to ensure that regulatory accounting data and related information filed by carriers are adequate, truthful, and thorough."<sup>1</sup> The attached report reflects the work of the Joint Conference between October 17, 2002 and October 6, 2003. The Joint Conference respectfully requests the Commission issue a Notice of Proposed Rulemaking seeking comment on the report and consider adopting the Joint Conference's recommendations.

Respectfully submitted,

The Honorable Kevin J. Martin, Commissioner  
Federal Communications Commission

The Honorable Michael J. Copps, Commissioner  
Federal Communications Commission

The Honorable Nancy Brockway, Commissioner  
New Hampshire Public Utilities Commission

The Honorable Terry Deason, Commissioner  
Florida Public Service Commission

The Honorable Rebecca A. Klein, Chairman  
Texas Public Utilities Commission

The Honorable Loretta Lynch, President  
California Public Utilities Commission

The Honorable Diane Munns, Chair  
Iowa Utilities Board

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<sup>1</sup> *Federal-State Joint Conference on Accounting Issues*, Order, 17 FCC Rcd 17025, para. 1 (2002) (*Convening Order*), see 47 U.S.C. § 410(b).

In the Matter of	)	
	)	
Federal-State Joint Conference	)	WC Docket No. 02-269
On Accounting Issues	)	

## RECOMMENDATION BY JOINT CONFERENCE

**By the Joint Conference: Commissioners Martin and Copps issuing separate statements. Commissioners Brockway, Deason, Klein, Lynch, and Munns agreeing, without separate statements.**

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## I EXECUTIVE SUMMARY

The Joint Conference requests that the Commission issue a formal Notice of Proposed Rulemaking (NPRM) seeking comment on the following recommendations:

► Modifications to Part 32:

1. The FCC should reinstate Account 5230, Directory Revenue, so that this line of business revenue can be monitored separately.
2. The FCC should reinstate Account 6621, Call Completion Services, Account 6622, Number Services, and Account 6623, Customer Services.
3. The FCC should reinstate the separate depreciation and amortization Accounts 6561-6565
4. The FCC should revise its Part 32 rules to add the following separate accounts:

Optical Switching  
Switching Software  
Loop and Interoffice Transport  
Interconnection - Revenue (with subaccounts for UNE's, Resale,  
Reciprocal Compensation and Interconnection Arrangements)  
Universal Service Support Revenue  
Universal Service Support Expense

► Affiliate Transactions Requirements.

1. The FCC should affirm the requirement for a comparison between net book cost and fair market value for the first \$500,000 of asset transfers.
2. The FCC should reverse its decision to permit ILEC discretion in valuing affiliate transactions.
3. The FCC should reinstate the threshold required to qualify for prevailing price valuation of affiliate transactions to 50 percent of sales of a particular asset or service to third parties.
4. The FCC should eliminate the centralized services exemption.
5. The FCC should maintain the current reporting requirements for nonregulated to nonregulated affiliate transactions and take no additional action at this time.

- 6 The FCC should apply its affiliate transactions rules to transactions between ILECs within the same holding company.
  - 7 The FCC should require BOCs, following the elimination of the affiliate and nondiscriminatory requirements of section 272, to maintain separate books of account for the provision of interexchange service and maintain an affiliate that provides in-region interexchange service that is subject not only to accounting review but also to certain safeguards.
- Reporting requirements and other issues:
- 1 If the requirement to collect local loop facilities as loop sheath kilometers on ARMIS Report 43-07 is retained, the FCC should also reinstate the reporting of sheath kilometer reporting requirement for some period
  - 2 The FCC should deny reconsideration petitions regarding the reporting of broadband infrastructure data in ARMIS Report 43-07, while continuing to evaluate whether the data collection should be expanded to a larger universe of carriers.
  3. The FCC should affirm that the amendment adopted to rule 32.11 of its accounting and reporting rules apply to all incumbent local exchange carriers as generally defined in section 251(h).

## II INTRODUCTION

On September 5, 2002, the Federal Communications Commission (FCC or Commission) issued a *Convening Order* establishing a Federal-State Joint Conference on Accounting Issues (Joint Conference), to “provide a forum for an ongoing dialogue between the Commission and the states in order to ensure that regulatory accounting data and related information filed by carriers are adequate, truthful, and thorough.”<sup>1</sup> According to the *Convening Order*, the Joint Conference, “will further this goal by facilitating cooperative federal and state review of regulatory accounting and related reporting requirements in order to determine their adequacy and effectiveness in the current market and make recommendations for improvement.”<sup>2</sup>

Subsequently, the Commission issued an *Order* that suspended implementation of four accounting and record keeping rule modifications adopted by the *Phase II Report and Order*. (1) the consolidation of Accounts 6621 through 6623 into Account 6620, with subaccounts for wholesale and retail; (2) the consolidation of Account 5230, Directory Revenue, into Account 5200, Miscellaneous Revenue; (3) the consolidation of the depreciation and amortization

<sup>1</sup> *Federal-State Joint Conference on Accounting Issues*, Order, WC Docket No. 02-269, FCC 02-240, para 1 (rel September 5, 2002) (*Convening Order*)

<sup>2</sup> *Convening Order* at para. 1

expense accounts (Accounts 6561 through 6565) into Account 6562, Depreciation and Amortization Expenses, and (4) the revised "Loop Sheath Kilometers" data collection in Table 11 of ARMIS Report 43-07.<sup>3</sup> The Commission concluded that further consideration of these changes before their implementation would advance the work of the Joint Conference.

On December 12, 2002, the Joint Conference issued a *Joint Conference Public Notice* with respect to its comprehensive review of regulatory accounting and related reporting requirements.<sup>4</sup> The *Joint Conference Public Notice* requested comment on a number of the issues that were addressed in the *Phase II Report and Order*. Specifically, comment was requested with respect to (1) the accounts requested by states but not added in Phase II; (2) the provisions of the *Phase II Report and Order* that were suspended by the Commission in its November 12, 2002 Order; (3) the provisions of issues raised by the outstanding petitions for reconsideration of the *Phase II Report and Order*; and (4) the *Phase II Report and Order* changes to affiliate transaction rules.

### III BACKGROUND

#### A History Of Phase II

In 1999, the Commission initiated a two-phased comprehensive review of its accounting rules and the related reporting requirements for incumbent local exchange carriers (ILECs) to keep pace with changing conditions in a competitive telecommunications industry. In Phase I, which concluded with the *Phase I Report and Order*, the Commission adopted accounting rule changes and reporting reform measures for the Automated Reporting Management Information System (ARMIS) that could be implemented quickly.<sup>5</sup> In 2000, the Commission released a *Phase II Notice* wherein it commenced a Phase II comprehensive, biennial review to further revise its rules and reporting requirements in the near term by streamlining the chart of accounts, revising the affiliate transactions rules, modifying other accounting rules, and streamlining the ARMIS reporting requirements.<sup>6</sup> Concurrent with the *Phase II Notice*, the Commission

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<sup>3</sup> *Federal-State Joint Conference on Accounting Issues, 2000 Biennial Regulatory Review—Comprehensive Review of the Accounting Requirements and ARMIS Reporting Requirements for Incumbent Local Exchange Carriers Phase 2, Jurisdictional Separations Reform and Referral to the Federal-State Joint Board, Local Competition and Broadband Reporting*, WC Docket No. 02-269 and CC Docket Nos. 00-199, 80-286, and 99-301, Order, FCC 02-309 (rel. November 12, 2002), FCC 03-141 (rel. June 24, 2003). The November 12, 2002, Order suspended implementation to July 1, 2002, the June 24, 2003, Order extended the suspension until January 1, 2004.

<sup>4</sup> *Federal-State Joint Conference on Accounting Issues, Request for Comment*, WC Docket 02-269, DA 02-3449 (Issued December 12, 2002) (*Joint Conference Public Notice*).

<sup>5</sup> *Comprehensive Review of the Accounting Requirements and ARMIS Reporting Requirements for Incumbent Local Exchange Carriers Phase I*, CC Docket No. 99-253, Report and Order. (*Phase I Report and Order*).

<sup>6</sup> *2000 Biennial Regulatory Review—Comprehensive Review of the Accounting Requirements and ARMIS Reporting Requirements for Incumbent Local Exchange Carriers. Phase 2 and Phase 3*, CC Docket No. 00-199, Notice of Proposed Rulemaking, FCC 00-364 (rel. October 18, 2000) at para. 1 (*Phase II Notice*).

undertook a Phase 3 review focusing on a broader examination of Part 32<sup>7</sup> and ARMIS reporting requirements for more significant deregulation.<sup>8</sup>

Subsequent to the release of the *Phase II Notice*, the Commission adopted the recommendation of the Federal-State Joint Board on Separations to impose an interim freeze of Part 36<sup>9</sup> cost allocation rules for price cap carriers and rate-of-return carriers.<sup>10</sup> Additionally, on June 8, 2001, the Commission released a further notice seeking further comment on proposed additions, consolidations, or eliminations of certain Class A and Class B accounts.<sup>11</sup>

The Phase II review concluded with the *Phase II Report and Order* in which the Commission adopted further streamlining measures to its accounting rules and reporting requirements.<sup>12</sup> These revisions were based on determinations that specific accounting rules and reports were no longer necessary or were outdated in the “pro-competitive, deregulatory” national policy framework for the telecommunications industry.<sup>13</sup> Specifically, the revisions were intended to “reflect a sharpened focus on ongoing regulatory needs in the areas of competition and universal service,”<sup>14</sup> and minimize the regulatory burdens and distortions that could undermine the development of new technology. Concurrently, in a related *Further Notice of Proposed Rulemaking*, the Commission sought to refresh the Phase 3 record by requesting comment on certain accounting and related reporting requirements identified for future reform.

The *Phase II Report and Order* eliminated many Part 32<sup>15</sup> accounts and reduced ARMIS reporting requirements for mid-sized local exchange carriers.<sup>16</sup> On its own motion, the

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<sup>7</sup> 47 C F R Part 32

<sup>8</sup> *Phase II Notice* at para. 2

<sup>9</sup> 47 C F R Part 36

<sup>10</sup> *Jurisdictional Separations and Referral to the Federal-State Joint Board*, CC Docket No. 80-286, Report and Order, FCC 01-162 (rel. May 22, 2001) (*Separations Freeze Order*)

<sup>11</sup> *2000 Biennial Regulatory Review—Comprehensive Review of the Accounting Requirements and ARMIS Reporting Requirements for Incumbent Local Exchange Carriers Phase 2 and Phase 3*, CC Docket No. 00-199, Commission Seeks Further comment in Phase 2 of the Comprehensive Review of the Accounting Requirements and ARMIS Reporting Requirements for Incumbent Local Exchange Carriers, DA 01-1403 (rel. June 8, 2001) (*Phase II Further Notice*). After reviewing the comments, the FCC sought further comment on streamlining Class A and Class B accounts

<sup>12</sup> *2000 Biennial Regulatory Review—Comprehensive Review of the Accounting Requirements and ARMIS Reporting Requirements for Incumbent Local Exchange Carriers Phase 2, Amendments to the Uniform System of Accounts for Interconnection, Jurisdictional Separations Reform and Referral to the Federal-State Joint Board, Local Competition and Broadband Reporting*, CC Docket Nos. 00-199, 97-212, 80-286, and 99-301, Report and Order in CC Docket Nos. 00-199, 97-212, and 80-286 (*Phase II Report and Order*), Further Notice of Proposed Rulemaking in CC Docket Nos. 00-199, 99-301, and 80-286, FCC 01-305 (rel. November 5, 2001) (*Further Notice of Proposed Rulemaking*).

<sup>13</sup> *Phase II Report and Order* at para. 2.

<sup>14</sup> *Id.* at para. 4

<sup>15</sup> 47 C F R Part 32

<sup>16</sup> *Phase II Report and Order* at para. 5

Commission issued limited reconsideration of the rules adopted in the *Phase II Report and Order* <sup>17</sup>

On March 8, 2002, BellSouth Corporation, SBC Communications Inc., and Verizon filed a joint petition for reconsideration of the *Phase II Report and Order*.<sup>18</sup> The petitioners asked that two newly created subaccounts - the wholesale and retail subaccounts to Account 6620, Services - be eliminated. The petitioners also requested that the Commission change the reporting of "Loop Sheath Kilometers" back to "Sheath Kilometers." The petitioners argued that the Commission should delay implementation of the relevant rule changes pending review of the arguments raised in the reconsideration petition. AT&T Corp. opposed both the petition for reconsideration and the request to delay implementation <sup>19</sup>

## B Biennial Review Standard

The biennial review of the accounting rules and the ARMIS reporting requirements was driven by section 11 of the Communications Act of 1934. That law, adopted in 1996, requires the FCC to review every two years those regulations that are "no longer necessary in the public interest as the result of meaningful economic competition between providers . . ."<sup>20</sup> On November 5, 2001, the Commission released its *Phase II Report and Order* to meet the biennial review requirements with respect to accounting and ARMIS reporting requirements.<sup>21</sup> The Commission appeared to define the public interest standard in section 11 as synonymous with federal purpose. Analysis of different accounts under the Phase II process was undertaken according to the "federal purpose" standard. In the Further Notice of Proposed Rulemaking, paragraph 207, the FCC stated "[w]e believe that, if we cannot identify a federal need for a regulation, we are not justified in maintaining such a requirement at the federal level."

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<sup>17</sup> 2000 Biennial Regulatory Review—Comprehensive Review of the Accounting Requirements and ARMIS Reporting Requirements for Incumbent Local Exchange Carriers, CC Docket No. 00-199, Order on Reconsideration, FCC 02-68 (rel. March 8, 2002) (*Order on Reconsideration*). The Commission reinstated Account 3400, Accumulated Amortization - Tangible, a Class B account, at the request of United States Telecom Association. At Sprint's request, the Commission clarified that mid-sized carriers are not required to file ARMIS 43-02 (USOA Report), 43-03 (Joint Cost Report), and 43-04 (*Separations and Access Report*). Finally, at the request of the Bell Operating Companies, the Commission extended the effective date of the changes to the Part 32 chart of accounts, and derivative changes to Parts 51 and 54 to January 1, 2003.

<sup>18</sup> Petition of BellSouth, SBC and Verizon for Reconsideration of Report and Order in CC Docket Nos. 00-199, 97-212, and 80-286 (filed March 8, 2002) (*Joint Petition for Reconsideration*). The Joint Petition also asked the Commission to reconsider its decision to collect certain new data concerning deployment of broadband facilities in ARMIS pending further consideration of broadband reporting requirements in Phase 3 of the proceeding. *Joint Petition for Reconsideration* at 1-11. In addition, SBC filed a separate petition for reconsideration seeking changes to the amended rule 32.11, 47 C.F.R. § 32.1, which is the rule that specifies which carriers are subject to regulated accounting requirements. SBC Communications, Inc. Petition for Reconsideration (filed March 8, 2002) (*SBC Reconsideration*).

<sup>19</sup> Opposition of AT&T Corporation to Petitions for Reconsideration, (filed May 15, 2002) (*AT&T Opposition*).

<sup>20</sup> 47 U.S.C. § 161.

<sup>21</sup> See, *Phase II Report and Order*.

In *Louisiana PSC*, the Supreme Court discussed the Commission's ability to impose accounting requirements pursuant to section 220 of the Communications Act.<sup>22</sup> Even though the case was decided prior to the Congress enacting the local competition provisions in 1996, the case nonetheless recognized that the realities of technology and economics make a clean parceling of responsibility between the state and federal jurisdictions difficult. The Court reasoned that virtually all telephone plant that is used to provide intrastate service is also used to provide interstate service. The Court stated, "[m]oreover, because the same carriers provide both interstate and intrastate service, actions taken by federal and state regulators within their respective domains necessarily affect the general financial health of those carriers, and hence their ability to provide service, in the other 'hemisphere.'"<sup>23</sup> The division of domestic telephone service neatly into two hemispheres, one comprised of interstate and the other made up of intrastate service, was further complicated by the 1996 Act.

The Supreme Court declined to specifically define the scope of the accounting jurisdiction under section 220. It stated it is possible that the section was to do no more than spell out the authority of the FCC over depreciation in the context of interstate regulation. But it also stated that it is similarly plausible that the section was addressed to the plenary authority of the FCC to dictate how the carriers' books would be kept for the purposes of financial reporting in order to ensure that investors and regulators would be presented with an accurate picture of the financial health of the carriers.<sup>24</sup>

These two possible purposes of section 220 become relevant in reviewing the FCC's application of the definition of "public interest" to its accounting requirements in its biennial review. The Commission appears to have applied the more limited purpose of section 220 discussed by the Court, that being whether the FCC uses the information in exercising specifically defined duties related to interstate service.

After the FCC finished its review and issued its order in 2001, the financial and accounting scandals that rocked the telecommunications industry began to surface. The economic impact on individual carriers as well as on the country as a whole has not been fully quantified but is known to be significant. The FCC "convened this Joint Conference on Accounting Issues to provide a forum for an ongoing dialogue between the Commission and the states in order to ensure that regulatory accounting data and related information filed by carriers are adequate, truthful and thorough."<sup>25</sup> The Joint Conference was charged to facilitate "cooperative federal and state review of regulatory accounting and related reporting requirements in order to determine their adequacy and effectiveness in the current market and make recommendations for improvements."<sup>26</sup> The Commission stated:

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<sup>22</sup> *Louisiana PSC v. FCC*, 476 U.S. 355 (1986) (*Louisiana PSC*).

<sup>23</sup> *Id.* at 360.

<sup>24</sup> *Id.* at 377-78.

<sup>25</sup> See *Covering Order* at para. 1.

<sup>26</sup> *Id.*

The Joint Conference will have a broad mandate to evaluate accounting requirements that state and federal regulators need to carry out their responsibilities. This analysis could include, among other things, an evaluation of current regulatory accounting rules, consideration of the scope of these rules, and an examination of any additions or eliminations of accounting requirements. The Conference may utilize existing federal and state data collection procedures and conduct hearings to collect information necessary to further the development of improved regulatory accounting and related reporting requirements and ensure that data filed by carriers are adequate, truthful, and thorough.

The effective date of several Phase 2 changes was also put on hold so the Joint Conference could reexamine the changes and make recommendations. These charges and responsibilities entrusted to the Joint Conference follow the broader purpose of section 220,<sup>27</sup> to ensure that investors and regulators are presented with an accurate picture of the financial health of the carriers

While under the *Louisiana PSC* case the states are free to prescribe their own accounting requirements and are not preempted by the FCC, it is apparent that viewing data on a limited state-by-state basis without the context of national data makes it very difficult to accurately measure the “financial health of the carriers.” It is also more burdensome to require fifty or more potentially different accounting requirements as opposed to collecting data at a national level. Thus, as a result of its work under the broad mandate of the *Convening Order*, the Joint Conference believes that the Commission may adopt accounting requirements to meet the needs of the states and other stakeholders.

#### IV. MODIFICATIONS TO PART 32

##### A Consolidation Of Directory Revenues (Acct. 5230) Into Miscellaneous Revenue (Acct. 5200)

**Issue:** Should the FCC reverse its decision to consolidate Account 5230, Directory Revenue, into Account 5200, Miscellaneous Revenue?

**Recommendation:** Yes. The FCC should reinstate Account 5230, Directory Revenue, so that this line of business revenue can be monitored separately.

The Telecommunications Act of 1996 established specific rules and regulations that allowed Regional Bell Operating Companies (RBOCs, also known as Bell Operating Companies (BOCs)) to enter lines of businesses that they had been prohibited from participating in at divestiture. Revenues derived from these affiliated lines of businesses are required to be tracked separately, whether an RBOC is operating under traditional rate of return, or using some form of alternative regulation. Before issuance of the Modified Final Judgment (MFJ)<sup>28</sup> in 1984, the

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<sup>27</sup> 47 U.S.C. § 220

<sup>28</sup> *United States v. Western Electric Co.*, 569 F. Supp. 990 (1983)

local Bell telephone companies published and distributed alphabetical and classified telephone directories (the white and yellow pages) within their service territories. The cost and revenues associated with those publications were considered part of the telephone company's operations. In other words, publication of telephone directories was part of the local telephone company's service obligations, and the revenues from directory publishing and advertising were used to defray the utility's revenue requirement.

Subsequent to divestiture, those directory operations were transferred to a non-regulated affiliate, with revenues for services rendered under these agreements booked to Account 5230, consistent with FCC (Part 32<sup>29</sup>) accounting rules, the Uniform System of Accounts for Telecommunications Companies (USOA). The intent was that ratepayers would continue to receive the economic benefit from the licensing, publishing, distribution and revenue sharing agreements. The revenues derived from the directory operations have flowed back to the BOC and have been reported in Account 5230, Directory Revenues. These revenues have been treated "above-the-line"<sup>30</sup> for intrastate revenue requirement determinations. Many of the states, in moving to alternative forms of regulation, have put in place an imputation of the Directory Revenues, which necessitates distinct and detailed accounts.

The *Phase II Report and Order* consolidated Account 5230, Directory Revenues, into Account 5200, Miscellaneous Revenue. Directory Revenues are created through a separate and distinct line of business and as such should be accounted for separately. The purpose of a "miscellaneous" account is to alleviate the need for hundreds of individual revenue accounts to account for small, insignificant amounts. Clearly, the amounts recorded for directory revenues are not insignificant. Directory revenues would often be one of the largest components recorded as miscellaneous revenue.<sup>31</sup>

The elimination of the Directory Revenues Account will result in the commingling of a variety of revenues into one reported amount. This would likely include revenues from retail, corporate operations, customer operations, and other incidental regulated revenue. For states still operating under rate of return regulation, as well as those using alternative forms of regulation, directory revenue is a source of controversy. The information provided by a separate accounting of directory revenues is necessary to the state regulators as they carry out the responsibility under the 1996 Act to protect consumers and competition against the incumbents' use of its local monopolies to gain a competitive advantage in the market for directory listings.<sup>32</sup>

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<sup>29</sup> 47 C.F.R. Part 32

<sup>30</sup> "Above-the-line" refers to those services that the Commission includes to calculate a carrier's revenue requirement when setting rates

<sup>31</sup> Comments of the Public Service Commission of Wisconsin to the Joint Conference Request for Comment, WC Docket No. 02-269 (*Wisconsin Comments*) at 5. Comments of the National Association of State Utility Consumer Advocates to the Joint Conference Request for Comment (*NASUCA Comments*), WC Docket No. 02-269, at 14

<sup>32</sup> Comments of AT&T Corp. to the Joint Conference Request for Comment, WC Docket No. 02-269, (*AT&T Comments*) at 14. See also, *NASUCA Comments* at 14.



B Consolidation Into One Services Account (6620) And Creation Of Wholesale/Retail Subaccounts

**Issue.** Should the Commission reverse its Phase II decision to consolidate Account 6621, Call Completion Services, Account 6622, Number Services, and Account 6623, Customer Services, into Account 6620, Services and create wholesale and retail subaccounts to the newly consolidated account?

**Recommendation:** Yes. The Commission should reverse its Phase II decision. In addition, the FCC should seek comment on other measures that could be used to achieve the *Phase II Report and Order* goals of 1) recognizing an increased importance of the wholesale versus retail distinction as competition develops in the local exchange market and 2) assisting the states in developing unbundled network element (UNE) rates that properly reflect the costs of providing a wholesale service. Finally, the FCC should direct the ILECs to quantify the burdens associated with each alternative

The Commission should seek comment on consolidating Accounts 6621, Call Completion Services (operator services), and 6622, Number Services (directory assistance), into one account and retaining Account 6623, Customer Services, as a separate account. Regarding the creation of separate wholesale and retail subaccounts, the Commission should request comment on whether modifying ARMIS Report 43-02 to require the reporting of the wholesale/retail percent of customer services expense (Account 6623) would provide sufficient information in determining costs of providing wholesale services rather than creating the new subaccounts in the Part 32<sup>33</sup> accounting rules. Because ARMIS Report 43-02 is reported on an operating company basis, ILECs should be required to report the wholesale/retail percent on an individual state basis. The wholesale/retail percentage would be determined annually on a study basis that ILECs already use in UNE proceedings. This will provide information that can be used to set UNE rates and develop the discount for resale rates, without the burdensome requirement of maintaining separate subaccounts and the need to separately journalize retail and wholesale components.

If wholesale/retail subaccounts are created, the Commission should also seek comment on the propriety of making the new subaccounts applicable only to Account 6623, Customer Services, inasmuch as operator services and directory assistance are not required to be offered at UNE rates. The FCC should seek comment on how to define and distinguish wholesale and retail customer services costs

The *Phase II Report and Order* concluded that Accounts 6621-6623 (Account 6621, Call Completion Services, Account 6622, Number Services, and Account 6623, Customer Services) should be consolidated into Account 6620, Services.<sup>34</sup> Further, the *Phase II Report and Order*

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<sup>33</sup> 47 C F R Part 32

<sup>34</sup> *Phase II Notice*, Appendix 3, p. 46, Appendix 5, p. 49. The *Phase II Notice* proposed the consolidation of the services accounts (accounts 6620-6623) into one account 6620. The *Phase II Notice* also sought comment on creating subaccounts for customer operations expense to separately record expenses associated with wholesale and

created wholesale and retail subaccounts for the consolidated account.<sup>35</sup> The FCC noted that the “wholesale versus retail distinction is important,” that this distinction likely would “increase in importance as competition develops in the local exchange market,” and that “[a]dding these new subaccounts w[ould] assist the states in developing UNE rates that properly reflect the costs of providing a wholesale service.” The FCC acknowledged that the wholesale versus retail distinction is important for customer service. This is because the per-line expenditure for customer service is higher at the retail level since competitive local exchange carriers (CLECs) (wholesale customers) do most of the customer service functions themselves. While ILECs opposed the addition of the wholesale and retail subaccounts and argued that the burden of adding the subaccounts outweighed any potential benefits, the *Phase II Report and Order* noted that the alleged burden had not been quantified.<sup>36</sup>

In the *Joint Petition for Reconsideration*, the ILECs seek elimination of the newly created wholesale and retail services subaccounts because they are unnecessary, conflict with existing regulations, and are extremely burdensome to implement.<sup>37</sup> The *Joint Petition for Reconsideration* requests a delay in implementing the new subaccounts until six months after publication in the Federal Register of the final ruling on the reconsideration petition.<sup>38</sup> Finally, the *Joint Petition for Reconsideration* seeks delay in implementing these subaccounts until after the FCC has concluded Phase 3 where various proposals could reshuffle Class A accounting and affect the creation of wholesale and retail subaccounts.<sup>39</sup>

The ILECs admit in the *Joint Petition for Reconsideration* that the distinction between wholesale and retail services is important in the marketplace, but argue that it is unnecessary and burdensome to carry that separation into expense accounting. Additionally, the ILECs assert that the accounting costs included in the wholesale and retail subaccounts would not be comparable to the forward-looking costs included in UNE cost studies. The *Joint Petition for Reconsideration* argues that operator services and directory assistance are not required to be offered at UNE rates. There is therefore no reason to create wholesale and retail subaccounts for these services that are provided and priced independently from UNEs.<sup>40</sup>

Regarding the burden of creating wholesale and retail subaccounts for the consolidated services account, the *Joint Petition for Reconsideration* asserts that the services encompassed in Account 6620 are provided to both retail and wholesale customers using the same systems and operators. Because the expenses are functionally the same, the ILECs assert that they are not easily broken into subaccounts for wholesale versus retail.<sup>41</sup> In order to comply with the *Phase II*

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retail services. The subaccounts were specifically proposed by the states to meet changing regulatory needs

<sup>35</sup> *Phase II Report and Order* at para. 64.

<sup>36</sup> *Id.*

<sup>37</sup> *See Joint Petition for Reconsideration* at 1.

<sup>38</sup> *Id.* at 2.

<sup>39</sup> *Id.* at 7.

<sup>40</sup> *Id.* at 3-4.

<sup>41</sup> *Id.*

*Report and Order*, the ILECs allege that they will have to undertake special studies to create subaccounts for the consolidated services account, either through allocation or by changing internal operating systems and procedures to allow for direct assignment. Either way, they argue, will be burdensome and time consuming.

Under the allocation method, Verizon estimates that it would take at least four to six months to structure and conduct special studies to create wholesale and retail subaccounts for the consolidated services account, costing close to \$3.5 million in additional implementation costs, and over \$2.5 million per year in ongoing costs.<sup>42</sup> These studies would be necessary to determine 1) the portion of the services expenses associated with the wholesale function and which are associated with the retail functions, 2) the portion of billing and collection costs are attributable to each, and 3) the portion of the employees' time that are related wholesale versus retail. However, in comments filed to the *Joint Conference Public Notice*, USTA, SBC, and Verizon note that FCC Rule Section 32.2(c) states that the regulated accounting system is based on actual costs, not allocated costs like that in Part 36<sup>43</sup> (Jurisdictional Separations Procedures) and Part 64<sup>44</sup>, Subpart I (Allocation of Costs).<sup>45</sup> In this respect, using a cost allocation approach to create wholesale and retail subaccounts would not be consistent with the FCC's accounting rules. SBC asserts that undertaking studies to allocate costs is unduly burdensome and costly. Furthermore, SBC argues that factors developed from studies performed during a prior period would be applied to current data, and therefore, would only reflect a representation of costs associated with wholesale and retail activities related to customer services rather than the actual costs incurred for such purposes.<sup>46</sup>

If operational system changes are made to segregate the expenses into wholesale and retail for the consolidated services account, BellSouth has estimated an 18-month implementation period at a cost of about \$12.5 million.<sup>47</sup> Existing billing systems would have to be separated and duplicated. In *ex parte* discussions, BellSouth explained that underlying accounting codes and methodology are already established to capture wholesale and retail expenses for customer services, Account 6623. However, operator services and directory assistance systems do not currently distinguish between wholesale and retail; there are currently no procedures or identifiers in place like there are with Account 6623. This will mean extensive and burdensome modifications to existing internal operations to create the methodology and tracking of separate wholesale and retail expenses.

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<sup>42</sup> *Id.* at 5-6.

<sup>43</sup> 47 C.F.R. Part 32.

<sup>44</sup> 47 C.F.R. Part 64.

<sup>45</sup> Comments of the United States Telecom Association, January 31, 2003, (*USTA Comments*) at 5-6; Comments of SBC Communications Inc., January 31, 2003, (*SBC Comments*) at 17; Comments of Verizon to Joint Conference Request for Public Comment, January 31, 2003, (*Verizon Comments*) at 18-20.

<sup>46</sup> *SBC Comments* at 16-17.

<sup>47</sup> *Joint Petition for Reconsideration* at 6.

In opposition to the *Joint Petition for Reconsideration*, AT&T argues that the petition provides no basis for reconsidering the conclusions of the *Phase II Report and Order*.<sup>48</sup> AT&T alleges that the *Joint Petition for Reconsideration* ignores the record supporting the new subaccounts as well as the FCC's conclusion that these new subaccounts will increase in importance as competition develops. Additionally, AT&T asserts that these subaccounts are important in assessing ILEC compliance with its duty "to offer for resale at wholesale rates any telecommunications service that the carrier provides at retail to subscribers."<sup>49</sup> AT&T alleges that total element long-run incremental cost (TELRIC) pricing of UNEs looks to "forward-looking economic cost-based pricing," but UNE pricing also reflects common costs, loading factors and other overhead costs attributable to the costs of operating a wholesale network. Routinely, those costs are assessed by reviewing ARMIS accounts based on the theory that historical ratios of such costs to investment may serve as a proxy (or at least a starting point) for estimating forward-looking levels of these costs. For this reason, the FCC's decision to create separate accounts for wholesale and retail services will assist the states in the development of UNE rates that properly reflect the costs of providing wholesale service.<sup>50</sup> Moreover, AT&T asserts that the *Joint Petition for Reconsideration* makes no additional effort to describe or quantify the burden this accounting requirement would impose.<sup>51</sup>

In reply to the *AT&T Opposition*, the ILECs argue that, while such costs may be used as a "starting point" for UNE rates or in determining resale rates, carriers must perform studies to determine these costs and set forth details of how the analyses were performed. The ILECs argue that the *Phase II Report and Order* will require studies to be undertaken on a more frequent basis and require carriers to journalize these costs on a monthly basis. Requiring monthly, journalized entries is inefficient for UNE and resale purposes because these proceedings generally do not take place every year. Moreover, no analysis has been performed to determine whether less burdensome measures could be used to achieve the stated goals.<sup>52</sup>

In its comments to the *Joint Conference Public Notice*, BellSouth suggests that if states need a wholesale component, the wholesale percentage determined on a study basis could be reported in ARMIS. This would serve the states alleged need for the information without causing ILECs to incur undue burdens of splitting these expenses between wholesale and retail for journalization on a monthly basis.<sup>53</sup> Having this data reported in ARMIS should reduce the amount of discovery in UNE filings. ILEC costs should be minimal since the procedures are already in place for these special studies and will not require the changing of internal operating

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<sup>48</sup> *AT&T Opposition* at 6.

<sup>49</sup> 47 U.S.C. § 251(c)(4)(A).

<sup>50</sup> *Id.* at 7. See also, *Phase II Report and Order* at para. 64, Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, First Report and Order, 11 FCC Rcd 15499, para. 691 (1996) (*Local Competition Order*) (explaining that "directly attributable costs" are relevant to pricing of UNEs, but that "costs associated with retail services" shall "not be included").

<sup>51</sup> *AT&T Opposition* at 8.

<sup>52</sup> Reply of BellSouth, SBC, and Verizon to AT&T's Opposition to Joint Petition for Reconsideration of Report and Order in CC Docket Nos. 00-199, 97-212, and 80-286, filed May 28, 2002, at 4-7.

<sup>53</sup> BellSouth Initial Comments to the Joint Conference Public Notice, (*BellSouth Comments*) at 11.

systems and procedures.<sup>54</sup> ARMIS reports cover a 12-month period and do not require monthly, journalized costs.

In summary, wholesale and retail data are important in assessing ILEC compliance with its duty “to offer for resale at wholesale rates any telecommunications service that the carrier provides at retail to subscribers.”<sup>55</sup> Wholesale and retail data are used in determining the appropriate discount for setting resale rates. With the requirement to resell wholesale services at a discount, data is needed regarding retail costs and what costs will be incurred when providing wholesale services.<sup>56</sup> ILEC retail services available for resale are priced on a wholesale basis. Wholesale prices are determined on the basis of subscriber retail rates, excluding portions attributable to marketing, billing, collection, and other costs that will be avoided by the ILEC. Avoided costs are included in Account 6623, Customer Services.<sup>57</sup> The Commission should be guided by its existing rules regarding the determination of avoided retail costs in setting wholesale rates.<sup>58</sup>

Additionally, wholesale and retail data are used in determining the appropriate mark-up for joint and common costs in determining UNE rates.<sup>59</sup> TELRIC pricing of UNEs looks to “forward-looking economic cost-based pricing,” but UNE pricing also reflects common costs, loading factors and other overhead costs attributable to the costs of operating a wholesale network. Wholesale costs are routinely assessed by reviewing ARMIS accounts based on the theory that historical ratios of such costs to investment may serve as a proxy (or at least a starting point) for estimating forward-looking cost levels.

The wholesale/retail breakdown for Accounts 6621, Call Completion Services (operator services) and 6622, Number Services (directory assistance) are not necessary because these services are not required to be offered at UNE rates.<sup>60</sup> Nonetheless, ILECs did not provide

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<sup>54</sup> *AT&T Opposition* at 7. See also, *Phase II Report and Order* at para. 64 and *Local Competition Order* (explaining that “directly attributable costs” are relevant to pricing of UNEs, but that “costs associated with retail services” shall “not be included”)

<sup>55</sup> 47 U.S.C. § 251(c)(4)(A)

<sup>56</sup> See *Wisconsin Phase II Comments*, December 21, 2000, at 7 and Attachment A

<sup>57</sup> Reply Comments of the Public Utilities Commission of Ohio in CC Docket Nos. 00-199, 97-212, 80-286, and 99-301 in the *Phase II Further Notice*, at 8

<sup>58</sup> 47 C.F.R. § 51.609 (d). In determining avoided costs, the Commission requires that the direct costs recorded in the services accounts (Accounts 6621, 6622, and 6623). Indirect costs may be included in wholesale prices only to the extent that the ILEC proves to a state commission that specific costs in these accounts will be incurred and are not avoidable with respect to services sold at wholesale, or that specific costs in these accounts are not included in retail prices of resold services

<sup>59</sup> See *Wisconsin Comments* at 7-8. For example, the Wisconsin Commission found in a SBC UNE proceeding that costs incurred regarding product definitions necessary to comply with the FCC rules were competition implementation costs. While SBC proposed that these costs be borne solely by wholesale customers as joint costs, the Wisconsin Commission determined that these costs should be considered as common costs and shared by all users of the network

<sup>60</sup> See *USTA Comments* at 5.

substantive evidence that it would be burdensome to provide a wholesale/retail breakdown for only Account 6623, Customer Services.

The Joint Conference recommends that the FCC reconsider its Phase II decision and seek comment on other measures that could be used to achieve the *Phase II Report and Order* goals of recognizing an increased importance of the wholesale versus retail distinction as competition develops in the local exchange market and assisting the states in developing UNE rates that properly reflect the costs of providing a wholesale service. ILECs should be requested to quantify the burdens associated with each alternative.

The Commission should seek comment on consolidating of Accounts 6621, Call Completion Services (operator services), and 6622, Number Services (directory assistance), into one account and retaining Account 6623, Customer Services, as a separate account. Regarding the creation of separate wholesale and retail subaccounts, the Commission should request comment on whether modifying ARMIS Report 43-02 to require the reporting of the wholesale/retail percent of customer services expense (Account 6623) would provide sufficient information in determining costs of providing wholesale services rather than creating the new subaccounts in the Part 32<sup>61</sup> accounting rules. Because ARMIS Report 43-02 is reported on an operating company basis, ILECs should be required to report the wholesale/retail percent on an individual state basis. The wholesale/retail percentage would be determined annually on a study basis ILECs already use in UNE proceedings and in keeping with the requirements of section 51.609<sup>62</sup>. This will provide information used in determining UNE rates, developing the discount for resale rates, as well as information regarding competition without the burdensome requirement of maintaining separate subaccounts and the need to separately journalize retail and wholesale components.

If wholesale/retail subaccounts are created, the Commission should seek comment whether the new subaccounts should be applicable only to Account 6623, Customer Services, since UNE rates are not required for operator services and directory assistance. In this case, a determination of what constitutes a wholesale and retail cost is needed. The FCC should seek comment on how to define and distinguish wholesale and retail customer services costs.

C. Consolidation Of Accounts 6561-6565 Into One Depreciation And Amortization Expense Account (6562)

**Issue:** Should the FCC reverse its decision to consolidate Accounts 6561-6565 into one Depreciation and Amortization Expense Account?

**Recommendation:** Yes. The Joint Conference recommends the FCC seek further comment related to the consolidation of these accounts and any possible adverse effects on potential rate proceedings at the state commissions

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<sup>61</sup> 47 C F R Part 32

<sup>62</sup> 47 C F R § 51.609

The USOA continues to be an essential regulatory tool for local, access, and UNE rate setting, price cap regulation, earnings monitoring, and or rate-of-return (ROR) proceedings for ILECs. Data compiled from records maintained in accordance with the USOA are used as the basis for all federal and state proceedings involving tariffs and costs for regulated carriers.<sup>63</sup> Where there is minimal to no competition, competitive forces alone will not govern the marketplace; therefore it may be necessary to continue regulation until competition forces declining prices.

The analysis of costs and determination of rate base sometimes differ between jurisdictions. As a result, segregation of the depreciation and amortization accounts continues to be needed by the states.<sup>64</sup> For example, the treatment of Property Held for Future Use, Account 6562, is often very contentious in a state ratemaking proceeding. For this reason, these expenses should be segregated rather than combined with other depreciation and amortization accounts. Maintaining these expenses in separate accounts while there remains a need for specific detail will be less burdensome than attempting to generate the data on a case-by-case basis.<sup>65</sup> The data will also be available on a timely basis, thereby allowing the FCC, states, and or court proceedings to move forward.

Although many jurisdictions have adopted various forms of alternative regulation to ROR, the fact is that some alternative regulation plans are earnings based, or require refunds, or provide options of returning to the ROR methods if price caps prove to be ineffective. The Commission should therefore re-establish the separate depreciation and amortization accounts (6561-6565) that were consolidated by the *Phase II Report and Order*.

#### D Addition Of Accounts

**Issue:** Should the FCC modify its Part 32<sup>66</sup> Rules to add the following separate accounts?

- Optical Switching
- Switching Software
- Loop and Interoffice Transport
- Interconnection – Revenue (with subaccounts for UNE's, Resale, Reciprocal Compensation and Interconnection Arrangements)
- Universal Service Support Revenue
- Universal Service Support Expense

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<sup>63</sup> Comments of the National Telecommunications Cooperative Association, filed January 31, 2003, (*NTCA Comments*) at pp 2-3

<sup>64</sup> *Wisconsin Comments* at p 6

<sup>65</sup> *BellSouth Comments* at pp. 8-9 BellSouth continues to maintain its Chart of Accounts so that depreciation and amortization expenses can be identified for state reporting purposes, but does not believe Price Cap companies should be required to report this detail in ARMIS

<sup>66</sup> 47 C F R Part 32.